



Arizona House of Representatives House Majority Research MEMORANDUM

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To: Joint Legislative Audit Committee

Re: Arizona Department of Financial Institutions

Date: November 1, 2013

Attached is the final report of the sunset review of the Arizona Department of Financial Institutions, which was conducted by the House of Representatives Financial Institutions and Senate Finance Committee of Reference on Monday, October 21, 2013.

This report has been distributed to the following individuals and agencies:

Governor of the State of Arizona
The Honorable Janice K. Brewer

President of the Senate
Senator Andy Biggs

Speaker of the House of Representatives
Representative Andy Tobin

Senate Members
Senator Steve Yarbrough, Co-chair
Senator Michele Reagan
Senator Bob Worsley
Senator Olivia Cajigas
Senator Robert Meza

House Members
Representative Kate Brophy McGee, Co-chair
Representative Jeff Dial
Representative David Livingston
Representative Rosanna Gabaldon
Representative Lydia Hernandez

DEC 30 2013

Arizona Department of Financial Institutions
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Senate Democratic Staff
Senate Research Staff
Senate Resource Center

Chief Clerk
House Republican Staff
House Democratic Staff
House Research Staff

**House of Representatives Financial Institutions and Senate Finance
COMMITTEE OF REFERENCE REPORT:**

ARIZONA DEPARTMENT OF FINANCIAL INSTITUTIONS

Background

Laws 1973, Chapter 32, established the Arizona Department of Financial Institutions (DFI), formally known as the State Banking Department, to execute all state laws relating to financial institutions and enterprises. DFI supervises and regulates 19 types of financial institutions or enterprises including state-chartered banks, state-chartered credit unions, collection agencies, loan originators, mortgage brokers and sales finance companies. Additionally, DFI investigates complaints filed by consumers against these entities and directs appropriate remedial action if the violations are substantiated.

Arizona Revised Statutes (A.R.S.) § 6-111 stipulates that the chief officer of DFI is the Superintendent who is appointed by the Governor and confirmed by the Senate. The Superintendent is statutorily authorized to supervise and examine state-chartered financial institutions and enterprises and ensure they are operating efficiently, safely and in compliance with applicable state and federal law (A.R.S. § 6-123). Currently, DFI serves approximately 8,000 entities licensed to conduct business in this state (www.azdfi.gov). In FY 2013-14, the baseline operating budget for DFI is approximately \$3.827 million with 58.1 FTE positions. DFI terminates on July 1, 2014, unless continued by the Legislature (A.R.S. § 41-3014.10).

Committee of Reference Sunset Review Procedure

The Committee of Reference held one public hearing on Monday, October 21, 2013, to review the Office of the Auditor General's performance audit, consider DFI's responses to the sunset factors and receive public testimony. See minutes for further information.

Committee of Reference Recommendations

The Committee of Reference recommended that the Legislature continue DFI for ten years.

Attachments

1. Letter from Representative Kate Brophy McGee requesting DFI's response to the sunset and agency factors.
2. DFI's responses to the sunset and agency factors pursuant to A.R.S. § 41-2954, subsections D and F.
3. Meeting Notice.
4. Minutes and handouts from the Committee of Reference meeting.

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COMMITTEES:
FINANCIAL INSTITUTIONS,
CHAIRMAN
HEALTH

DISTRICT 28

Arizona House of Representatives Phoenix, Arizona 85007

July 9, 2013

Lauren W. Kingry
Superintendent of Financial Institutions
Arizona Department of Financial Institutions
2910 N. 44th Street, Suite 310
Phoenix, Arizona 85018

Dear Superintendent Kingry:

The sunset review process prescribed in Title 41, Chapter 27, Arizona Revised Statutes, provides a system for the Legislature to evaluate the need to continue the existence of state agencies. During the sunset review process, an agency is reviewed by a legislative committee of reference. On completion of the sunset review, the committee of reference recommends to continue, revise, consolidate or terminate the agency.

The Joint Legislative Audit Committee (JLAC) has assigned the sunset review of the Arizona Department of Financial Institutions to the committee of reference comprised of members of the Senate Finance Committee and the House of Representatives Financial Institutions Committee. JLAC has directed the Auditor General to conduct a performance audit of the Arizona Department of Financial Institutions.

Pursuant to A.R.S. § 41-2954, the committee of reference is required to consider certain sunset factors in deciding whether to recommend continuance, modification or termination of an agency. In addition to the 12 sunset factors, which are addressed in the Auditor General performance audit, please provide your agency's written response to the required factors as listed below:

1. An identification of the problem or the needs that the agency is intended to address.
2. A statement, to the extent practicable, in quantitative and qualitative terms, of the objectives of such agency and its anticipated accomplishments.
3. An identification of any other agencies having similar, conflicting or duplicate objectives, and an explanation of the manner in which the agency avoids duplication or conflict with other such agencies.
4. An assessment of the consequences of eliminating the agency or of consolidating it with another agency.

Superintendent Lauren W. Kingry

July 9, 2013

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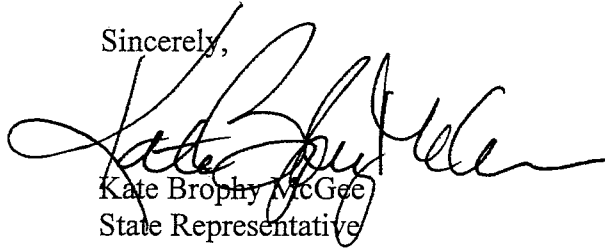
5. The extent to which the agency potentially creates unexpected negative consequences that might require additional review by the committee of reference, including increasing the price of goods, affecting the availability of services, limiting the abilities of individuals and businesses to operate efficiently and increasing the cost of government.

Your response should be received by September 1, so we may proceed with the sunset review and schedule the required public hearing. Please submit the requested information to:

Virginia (Ginna) Carico
Arizona House of Representatives
1700 West Washington
Phoenix, Arizona 85007

Thank you for your time and cooperation. If you have any questions, please feel free to contact me at (602) 926-4486 or Ginna Carico, the Financial Institutions Committee Research Analyst, at (602) 926-3147.

Sincerely,

A handwritten signature in black ink, appearing to read 'Kate Brophy McGee', is written over a printed name and title.

Kate Brophy McGee
State Representative

cc: Senator Steve Yarbrough, COR Co-Chair
Bill Ritz, Senate Finance Analyst



ARIZONA DEPARTMENT OF FINANCIAL INSTITUTIONS

Lauren W. Kingry
Superintendent of Financial Institutions

Janice K. Brewer
Governor

August 30, 2013

The Honorable Kate Brophy McGee
Chairman, Financial Institutions Committee
Arizona House of Representatives
1700 W. Washington Street
Phoenix, Arizona 85007

Representative Brophy McGee:

In response to your July 9, 2013 correspondence, the Arizona Department of Financial Institutions respectfully submits its response to five Sunset Factors that are required in addition to the twelve factors, which are addressed in the Auditor General performance audit as prescribed in A.R.S. §41-2954.

Regards,

A handwritten signature in black ink, appearing to read "Lauren W. Kingry", written over a horizontal line.

Lauren W. Kingry
Superintendent

cc: Senator Steve Yarbrough, COR Co-Chair
Bill Ritz, Senate Finance Analyst
Ginna Carico, House Financial Institutions Analyst

LWK: ld
Enclosure

STATUTORY REPORT PURSUANT TO A.R.S §41-2954(F)

1. Identification of the problem or the needs that the agency is intended to address.

Established as the State Banking Department in 1973, the agency was renamed the Department of Financial Institutions in 2006 to more accurately reflect the industries it serves. The purpose of the Department of Financial Institutions ("DFI") is to safeguard the public welfare by protecting the financial assets of the citizens of Arizona by executing the laws of this State relative to financial institutions and enterprises. The DFI ensures the safety and soundness of the financial services industry in Arizona and serves over 10,000 individuals and entities licensed to conduct business in the State as well as Arizona citizens that receive these services.

2. A statement, to the extent practicable, in quantitative and qualitative terms, of the objectives of such agency and its anticipated accomplishments.

The Department of Financial Institutions is charged with enforcing the laws that govern this State relating to financial institutions, enterprises and all applicable entities and individuals.

3. Identification of any other agencies having similar, conflicting or duplicative objectives, and an explanation of the manner on which the agency avoids duplication or conflict with other agencies.

No other agency has similar objectives

4. An assessment of the consequences of eliminating the agency, or of consolidating it with another agency.

Elimination of the Department of Financial Institutions would increase public exposure to deceptive practices of financial enterprises and reduce Arizona's control over financial institutions. Elimination of the DFI would ensure the delegation of duties transferred to the federal government. Consolidation could be achieved if confidentiality of records, liability, verification, and revenue issues could be resolved. Under these circumstances it is not in the State's best interest to consolidate the Department of Financial Institutions.

5. The extent to which the agency potentially creates unexpected negative consequences that might require additional review by the committee of reference, including increasing the price of goods, affecting the availability of services, limiting the abilities of individuals and businesses to operate efficiently and increasing the cost of government.

It is not believed that the agency creates any unexpected negative consequences that would require further review by the committee at this time.

ARIZONA DEPARTMENT OF FINANCIAL INSTITUTIONS SUNSET REVIEW – 2013

Factors for Consideration A.R. S. § 41-2954.D

- 1. The objective and purpose in establishing the agency, board, or commission and the extent to which the objective and purpose are met by private enterprises in other states.**

The State of Arizona Banking Department was created by statute during a Special Session of the Fifth Legislature on April 10, 1922. With the support and urging of the Arizona Credit Union League, A.R.S. § 6-110 was amended by Laws 2004, Ch. 188, § 3 to change the Department name to the Arizona Department of Financial Institutions, which became effective January 1, 2006.

The purpose of the Department is to safeguard public welfare by protecting the financial assets of the citizens of Arizona by executing the laws of this State relative to financial institutions and enterprises.

To memorialize that purpose, the Department adopted a revised mission statement:

To license, examine, and supervise Financial Institutions, in compliance with State law, to ensure safety for the Arizona consumer and soundness for the Arizona business.

Operationally, the Department is divided into four divisions:

- Financial Institutions – State chartered banks, credit unions, savings and loans, trust companies, trust divisions, and the examination and supervision of all included.
- Financial Enterprises – Performs the examination and supervision of all non-depository licensees licensed by DFI.
- Licensing - Advance fee loan brokers, banks (state chartered), collection agencies, commercial mortgage bankers, commercial mortgage brokers, consumer lenders, credit unions (state chartered), debit management companies, escrow agents, money transmitters, mortgage bankers, mortgage brokers, motor vehicle dealers, premium finance companies, sales finance companies, savings and loan associations, trust companies, trust divisions, and loan originators.
- Administration – Personnel, budget, payroll, information technology.

The Arizona Department of Financial Institutions is charged with the licensing, examination, supervision and regulation of state-chartered financial institutions and

enterprises. The Superintendent is responsible for ensuring the safety and soundness of state-chartered financial entities and verifying compliance with applicable state and federal laws. The Department also investigates complaints that are filed by consumers against licensed entities where violations of state law or rules have been alleged, and directs appropriate remedial action if the violations are substantiated. The Department licenses approximately 8,600 entities to conduct business in the State. The statutes that govern these entities are Arizona Revised Statutes Title 6, Title 32 (Chapter 9) and Title 44 (Chapter 2.1).

The number of licensees has increased dramatically since 2003, from 3,260 to the current total of 8,565 as of September 6, 2012. This is an increase of 5,305 or 163 percent is largely due to legislation passed in 2010 requiring loan originators to be licensed by the Department. Exhibit "A" ("License Activity Summary") lists the 19 entities that the Department licenses.

2. The extent to which the agency, board, or commission has met its statutory objective and purpose and the efficiency with which it has operated.

Historical Agency Performance

Through FY 2008, DFI absorbed the increase in regulated companies using automation, cross training, and staff overtime where available. Unfortunately, these strategies had limitations and resulted in backlogs in licensing, consumer affairs, and mortgage examinations; delays in processing and responding to consumer complaints; and protracted examinations and investigations. Severe budget/staff reductions over the past four fiscal years exacerbated the problem. For FY 2013, DFI received reasonable additions to its budget, directed at mission critical functions; to maintain safe and sound banks, credit unions and other financial services, and to better protect consumers. Despite these additional resources, staffing levels have not kept pace with industry growth.

Exhibit "B" ("Doing More With Less, Fiscal Years 2003-2012") compares the growth in regulated licensees against DFI authorized staff over the past decade. The following growth rates occurred during this timeframe:

- 157% increase in the number of licensees;
- 15% increase in the number of full time employees (FTE);
- 126% increase in the number of licensees per FTE.

Despite the additional FTE authorized for the new loan originator licensing program (Financial Services Fund) the number of licensees per FTE has more than doubled since FY 2009. While the number of licensees (excluding loan originators) has declined during that time period, the addition of 5,320 licensed Loan Originators caused the number of licensees per FTE to jump to a staggering 149, from 64 just three years earlier. That

number is projected to grow to 162 per FTE for FY 2013 (Note: when based on 48 actual “funded” FTE, the projected number spikes to 196 for FY 2013.

Impact of Budget Cuts on Examination Team

Prior to the FY 2009 budget cuts, DFI was appropriated a total of 57.1 FTE – including 30 examiner positions (24 of which were filled). DFI also had 8 examiners being paid out of non-appropriated funds - for a total of 32 filled examiner positions. The combined impact of FY 2009 and FY 2010 budget cuts reduced the number of filled examiner positions to its current level of 22 - down 31 percent from the 32 in place before budget cuts began - for over 8,500 current license holders. Exhibit “D” illustrates the severe impact that aggregate budget reductions have had on the Department’s examination team.

Due to the lack of adequate resources, DFI has been unable to comply with some of the mandatory examination cycle for licensees. In fact, since the Department was unable to meet acceptable examination frequency and leadership guidelines for its state-chartered Banks and Credit Unions, its accreditation with the Conference of State Bank Supervisors (CSBS) and the National Association of State Credit Union Supervisors (NASCUS) was suspended. However, it’s accreditation with CSBS has since been reinstated.

The Department needs more examiners to be able to comply with the statutorily required examination schedule and supervise more “troubled” licensees. Furthermore, it needs to be able to better compensate these examiners. Turnover is less of a problem today than it has been historically, largely due to the anemic job market. But, the Department must be able to compete with both the federal and private sectors if it is to attract and retain qualified employees.

Given limited resources, the Department continues to explore ways to operate more efficiently. Conducting examinations-by-mail and, more recently, instituting an E-exam program, on some of its better-rated or minimal activity financial enterprises (collection agencies and mortgage brokers) reduces on-site time at the licensees. These procedures enable the Department to allocate more resources to “troubled” licensees. The agency also has adopted a “risk-focused” approach in its examinations that concentrates on inherent risks.

The Department continues to effectively deal with the impact of the financial crisis and housing collapse on the regulated community. Although there were still many bank failures across the country over the past year, since June 2011 there has only been one failure of an Arizona State-chartered bank. The one receivership currently being administered by the Department (a former mortgage banker) is expected to be closed by the end of FY 2013.

Impact of Budget Cuts on Licensing Division

A 50 percent reduction in Licensing Division staff (from 6 to 3 CSR's) created a significant backlog in processing licensing applications and related maintenance items. This hindered DFI's ability to meet statutorily required timeframes for processing license applications. This failure requires, by Arizona law, that the Department refund application fees to those applicants. This loss of funds directly impacts the State's revenue. The chart below, illustrates the impact to the general fund since 2007:

FYE	# of Applications	Total Refunds (\$)
2007	15	16,800
2008	9	9,700
2009	9	9,000
2010	11	10,800
2011	39	41,200
2012	1	800

The Department has recently implemented better control procedures surrounding the processing of license applications and maintenance items. The effectiveness of this new process is evidenced by the decline in the number of refunds required in FY 2012.

Loan Originator Licensing Program – Under A.R.S. Title 6, Chapter 9, Article 4, any person acting as a loan originator required a license from DFI beginning July 1, 2010. This new law also provided a financial structure that allows the Loan Originator licensing program to be self-sustaining and minimize support from the General Fund. The Loan Originator Licensing unit is adequately funded and staffed. This is evidenced by the ability of the unit to approve 1,447 new license applications in FY 2012 in an average of only 2 days per application.

Performance Measures

The Department has established various "Performance Measures" to assess its effectiveness and compliance with statutory requirements, including customer satisfaction levels. In order to assess customer satisfaction, surveys are sent to license applicants, complainants, and those licensees that have been examined. In addition to being a valuable management tool, the data is submitted to the Governor's Office of Strategic Planning & Budgeting on an annual basis. The data confirms improvement in the Department's ability to meet its objectives and purpose in those areas affected by budget cuts. Below are highlights of the FY 2012 data, clearly demonstrating the agency's customer commitment:

- 96% of licensing customers indicated receiving good or better service
- 100% of examination customers indicated receiving good or better service
- 74% of consumer affairs customers receiving good or better service
- 96% of home office license applications approved within 45 days
- 74% of regular complaints resolved within 30 days

Lastly, it is important to point out that the Department purchased a new licensing/MIS system, to replace a system (BDIS) which is antiquated and no longer supported by the vendor. Implementation activities are still underway. This new system will modernize and bring efficiencies to the Department's operations, including better reporting capabilities. There is concern however that the delays by the vendor may cause there to be some difficulties in finalizing this conversion plan.

3. The extent to which the agency, board, or commission serves the entire State rather than specific interests.

Agency services are provided for the benefit of the general public and its stakeholders. The public and the financial services industry benefit from the existence of the Department. The public benefits from regulatory activities that ensure compliance and enforcement of Arizona Revised Statutes. The industry benefits from these uniform regulations applied to all licensees in addition to being protected under Arizona state law.

The functions of the Department signify its commitment to the public interest:

- Investigation of New Applicants – the review includes a background check (personal history and financial statements, a credit report and an FBI report) on the primary license applicants, the financial condition of the entity to determine solvency and capital requirements, fidelity/surety bond documentation and a review of work experience and references.
- Examination of Licensees – in accordance with statute, regular examinations are conducted to confirm the safety and soundness of the licensee's business and its compliance with applicable laws. Licensees with serious financial or operational problems are identified, counseled and disciplined as necessary. The Department also performs off-cycle visitations or examinations of problem licensees.
- Investigation of Unlicensed Activity – such activity is called to our attention by other licensees, a customer complaint or as a result of an examination of another licensee. An investigation is conducted, often resulting in issuance of a Cease and Desist Order and/or requiring the business to obtain a license to remain in business in this state and/or the imposition of a civil money penalty. These investigations benefit the businesses that are licensed and subject to examination and regulation, helping to prevent unfair competition. Consumers also benefit as these cease and desist orders are immediately placed on our web site.
- Resolution of Consumer Complaints/Inquiries – the Department's Consumer Affairs Division investigates consumer complaints against licensed entities. A consumer complaint may lead to a full-scale investigation or examination. In

addition, this section responds to inquiries from the public regarding its rights and recourse against unfair practitioners. Consumers may receive refunds from companies who have violated Arizona law.

The Department has a number of administrative, disciplinary and enforcement actions and remedies at its disposal should it find it necessary to take action against its licensees and does not hesitate to do so when the public interest is threatened or jeopardized:

1. Written Agreements
 - a. Memorandums of Understanding (banks)
 - b. Letters of Understanding & Agreement (credit unions)
2. Cease & Desist Orders
3. Civil Money Penalties
4. Consent Agreements
5. Removal and/or Prohibition Orders
6. Injunctive Actions – Court Orders
7. Notice of Hearings
8. License Suspensions or Revocations
9. Receiverships

The Department provides oversight of institutions and enterprises during their earlier years. Banks in particular undergo a six-month visitation and then their first annual examination. During this de novo stage (3 years) all examinations are done jointly with the federal regulators, either the Federal Deposit Insurance Corporation or the Federal Reserve Bank. A Watch List for all entities is updated quarterly for institutions and on an as-needed basis for enterprises. Quarterly review meetings attended by all examiners, managers and senior management are conducted for institutions wherein call reports and other financial data are scrutinized for at-risk developments including rampant asset growth, increasing numbers of delinquent loans, and questionable investments. These procedures are aimed directly at protecting the public interest and avoiding the collapse of any entities.

The Department also fields calls and letters from the public on entities that the agency does not regulate. Department staff directs these individuals to the proper regulating authority.

The Department assists individuals dealing with large interstate banks. Customers of those institutions are frequently connected with the Consumer Affairs Division of the Department and helped with matters over which we have no authority or mandate. Assisting and educating those that contact the Department benefits the residents of Arizona.

The Department has conducted presentations to industry professionals, community organizations, educational institutions, trade associations, and the general public in the interest of creating a more informed State. The Superintendent and senior management has presented to mortgage brokers, mortgage bankers, loan originators, escrow agents,

collection agencies, land title, motor vehicle dealers, and other interested groups and associations. It is a goal of the Superintendent to remain available to address groups and individuals concerned with issues that affect them. A better-informed public is the best offset to predatory practices. The Department periodically issues "Regulatory Alerts" or "Regulatory Bulletins" as-needed to advise the public and financial industry of important developments.

The Department has taken steps to meet with industry officials throughout the year to discuss potential legislation and issues that may be affecting the industry. The Department generally takes a neutral stance on legislative issues because making laws is not a primary responsibility, but if a threat to public interest or presents itself the Department will intervene appropriately.

4. The extent to which rules adopted by the agency, board, or commission are consistent with the legislative mandate.

A. Rules review

The Department is currently undergoing a rules review of five rules. These will be placed on the Governor's Regulatory Review Council's October 2, 2012 agenda. Exhibit "F" ("Notice of Final Rulemaking") indicates the proposal. The Department has enacted a minimal number of rules over the past 3-5 years due to the Governor's moratorium on rule making by Executive Order since January 22, 2009. This moratorium was extended on June 26, 2012 through December 31, 2014.

R4-20-1301, R4-20-1302, R4-20-1303, R4-1304, and R4-1305 were created by emergency rulemaking at 16 A.A.R. 839, effective April 27, 2010 for 180 days. These sections were renewed by emergency rulemaking and amended at 16 A.A.R. 2165, effective October 24, 2010 for 180 days expiring April 21, 2011.

B. Authority to make rules.

The legislature has vested the Superintendent with broad rule-making authority. Pursuant to A.R.S. § 6-123, "The Superintendent may, in accordance with Title 41, Chapter 6, adopt rules necessary or appropriate to administer, enforce and accomplish the purposes of this Title." As the term is used in § 6-123, "Title" includes title 6, title 32, chapter 9, and title 44, chapter 2.1. The Department believes its rules are consistent with the Legislative mandate, and that it has sufficient authority to make all rules necessary to administer, enforce, and accomplish the purposes of the statutes it enforces.

C. Review by the Governor's Regulatory Review Council.

Under the authority of A.R.S. § 41-1052, the Governor's Regulatory Review Council ("G.R.R.C") reviews all rules proposed by the Department to ensure that each Section meets the following criteria:

1. The economic, small business and consumer impact statement contains the information, data and analysis prescribed by A.R.S. § 41-1055.
2. The economic, small business and consumer impact statement is generally accurate.
3. The probable benefits of the rule outweigh the probable costs of the rule.
4. The rule is clear, concise and understandable.
5. The rule is not illegal, inconsistent with legislative intent or beyond the agency's statutory authority.
6. The agency adequately addressed the comments on the proposed rule and any supplemental proposals.
7. The rule is not a substantial change, considered as a whole, from the proposed rule and any supplemental notices.
8. The preamble discloses a reference to any study relevant to the rule that the agency reviewed and either did or did not rely on in the agency's evaluation of or justification for the rule.
9. The rule, if it imposes new fees, does so under specific statutory authority.

D. Ensuring that rules are promulgated

In addition to review by the G.R.R.C, the Department's Legislative Liaison monitors enacted legislation and reviews rules and the rulemaking process to determine if changes are needed in rule. Additionally, it is an objective of the Department to maintain open communication with G.R.R.C staff.

5. **The extent to which the agency, board, or commission has encouraged input from the public before adopting its rules and the extent to which it has informed the public as to its actions and the expected impact on the public.**

A. Informal discussions.

The Department informs affected industries of all proposed changes to rules and provides the general public with all information required by law concerning its rulemaking activity. When requested, meetings are scheduled with interested parties and their legal representatives to solicit preliminary comment on proposed rules.

B. Compliance with Arizona's Administrative Procedure Act.

Following these preliminary meetings and discussions, and to comply with state law, the Department publishes a Notice of Proposed Rulemaking in the Arizona Administrative Register to give interested parties a chance to comment on the proposed revisions. After the statutory public comment period ends the Department submits a Notice of Final Rulemaking to G.R.R.C. If and when G.R.R.C approves the final rulemaking, the Department publishes a Notice of Final Rulemaking with the Secretary of State's Office in the Arizona Administrative Register to give interested parties notice of the revised Sections' to be heard at the council meeting.

6. **The extent to which the agency, board, or commission has been able to investigate and resolve complaints that are within its jurisdiction.**

Arizona Revised Statutes provide the authority under which the Superintendent investigates and resolves complaints against all licensee types under his/her jurisdiction. The Superintendent has the authority to investigate violations of the licenses that the Department supervises.

The Consumer Affairs Division of the Department is responsible for the processing of complaints. There are currently three full-time examiners who respond to written complaints and telephone inquiries. A large number of telephone inquiries can be resolved without the filing of a formal complaint. In those instances, the examiner provides information to the consumer about contacting the proper agency to direct the complaint. In many instances consumers simply wish to know if a specific transaction may have violated any section of the Titles that the Department oversees. The Department cannot resolve some complaints because they require litigation in order to determine the responsibility of the parties involved in the transaction. However, a significant number do result in the consumer filing a written complaint and are reviewed

to determine compliance with applicable law and the Department's ability to assist in its resolution.

Upon receipt of a written complaint it is assigned to an examiner who notifies the complainant of its receipt and the Department's intervention. At the same time, the licensee is notified of the complaint and is required to provide its response to the allegations. Once the licensee responds, the examiner evaluates its contents and determines whether it is a matter in which the Department can intercede within its authority under the applicable statutes. The complainant is advised in writing of the Department's conclusion and the licensee is also advised.

Routine customer complaints should be resolved within thirty days. This time-line is based upon several factors that include the processing and analysis period by Department staff as well as the licensee's timeliness in responding to the inquiry. Typically, the licensee is afforded ten days to respond. However, some complaints require additional time to resolve due to the age of the transaction or its complexity. The number of complaints resolved average approximately 900 per year.

7. The extent to which the Attorney General or any other applicable agency of state government has the authority to prosecute actions under the enabling legislation

A. Violations and Penalties Established by Law.

Upon the request of the Superintendent, the Attorney General has the obligation and authority to prosecute actions on behalf of the Department. Title 6¹ provides the Attorney General with a complete range of options to prosecute violations of the Title, bring civil actions to enjoin the violation of the Title, and prosecute or defend all actions resulting from enforcement of the Title. Further, the Title contains various statutes which provide for criminal sanctions for certain conduct. Some of these provisions are as follows:

1. A.R.S. § 6-133(A) provides that any person who knowingly violates any provisions of the Title or any Rule or Order issued or promulgated by the Superintendent is guilty of a Class 6 felony.
2. A.R.S. § 6-133(B) provides that any person who knowingly makes any false statement, misrepresentation or false certification in any application, record, report, plan or other document filed or required to be

¹Pursuant to A.R.S. § 6-101(17), references to the "Title" include Title 6 (A.R.S. § 6-101 *et seq.*), Title 32, Chapter 9 (A.R.S. § 32-1001 *et seq.*), and Title 44, Chapter 2.1 (A.R.S. § 44_281 *et seq.*).

maintained by the Title with intent to deceive the Superintendent is guilty of a Class 3 felony.

3. A.R.S. § 6-133(C) provides that any person who knowingly makes any false entry or omits a material entry in any record, report or statement of a licensee with intent to injure or defraud the licensee or to deceive the Superintendent is guilty of a Class 3 felony.
4. A.R.S. § 6-134 provides that any person who knowingly makes, circulates or transmits to another, a false statement or rumor which is derogatory of the financial condition or solvency of any bank, savings and loan association or credit union is guilty of a Class 2 misdemeanor.

In addition, statutes governing specific types of licenses provide for criminal sanctions for certain conduct. Some of these provisions are as follows:

1. For Savings and Loan Associations: A.R.S. § 6-484 provides that a person using a name embodying any combination of the words “building and loan association” or “savings and loan association,” or acting as agent for that person, is guilty of a Class 2 misdemeanor, unless complying with the provisions of Title 6.
2. For Escrow Agents: A.R.S. § 6-837(C) provides that any person who knowingly fails to produce records or who obtains information under A.R.S. § 6-837(A) or (B) is prohibited from releasing such information but does release such information is guilty of a Class 2 misdemeanor.
3. For Trust Companies: A.R.S. § 6-860(C) makes a similar prohibition against failing to produce records and releasing information obtained pursuant to A.R.S. § 6-860(A) or (B) as guilty of a Class 2 misdemeanor.
4. For Money Transmitters: A.R.S. § 6-1241(Q) states that a person who refuses to permit any lawful investigation by the superintendent, a county attorney or the attorney general or who refuses to make records available to the superintendent, a county attorney or the attorney general pursuant to subsection H of this section is guilty of a class 6 felony.
5. For Collection Agencies: A.R.S. § 32-1056(A) states that a person operating a collection agency without a license shall be guilty of a Class 1 misdemeanor. A.R.S. § 32-1056(B) states that a licensee violating the provisions of A.R.S. § 32-1055 or the rules and regulations adopted pursuant to this chapter shall be subject to revocation of license and shall be guilty of a Class 1 misdemeanor.

B. Imposition of Civil Penalties.

The Superintendent has the power to assess civil penalties in an amount of not more than \$5,000 against a person for any knowing violation of any provision of the Title or of any Rule or Order adopted or issued pursuant to this Title. Each day of violation constitutes a separate offense. If the assessment is not paid within thirty days, the Attorney General, on request of the Superintendent, shall bring action in Superior Court. On the finding of a knowing violation, the Court may enforce the civil penalty imposed by the Superintendent or may impose a different civil penalty in an amount it deems appropriate for each violation.

C. Administrative Actions.

1. Cease and Desist Orders

If it appears to the Superintendent that any person has engaged, is engaging in, or is about to engage in any act, practice or transaction which constitutes a violation of the Title or any Rule or Order of the Department, the Superintendent may issue an order directing that person to cease and desist from engaging in the act, practice or transaction or doing any act in furtherance of the act, practice or transaction and to take appropriate affirmative action.

2. Hearings

Arizona Revised Statutes, Title 6 contains numerous provisions relating to the granting, denying, revoking or suspending of a permit certificate or license provided under the Title. Disciplinary actions against licenses are also included in proceedings that are conducted in accordance with the Uniform Administrative Hearing Procedures Act (A.R.S. § 41-1092 *et seq.*). Administrative hearings are held before an Administrative Law Judge at the Office of Administrative Hearings. The Department of Financial Institutions is represented by the Attorney General at those hearings. The Administrative Law Judge makes a recommended decision to the Superintendent. However, the Superintendent makes the final administrative decision in the matter. Parties may appeal a final administrative decision pursuant to Title 12, Chapter 7, Article 6 in the Superior Court. The Department of Financial Institutions is represented by the Attorney General at these appeal hearings. An Appeal may also be made to the Court of Appeals and the State Supreme Court.

3. Proceeding for Officer Removal

The Superintendent has the authority to remove or suspend from office or prohibit from participating in any of the affairs of a licensee, any

director, officer or other person participating in the conduct of the affairs of the licensee, if he finds that person has engaged in any activity delineated in A.R.S. § 6-161(A). After the mortgage problems in 2005 and 2006, a number of mortgage and escrow persons were successfully removed from those industries.

D. The Attorney General has Adequate Authority to Prosecute Actions under the Department's Statutes.

The Attorney General's Office has the responsibility of prosecuting the Department's cases, both administratively and judicially. It is believed that the Attorney General has a sufficient level of prosecutory authority to meet Department needs.

8. The extent to which the agency, board or commission has addressed deficiencies in its enabling statutes which prevent it from fulfilling its statutory mandate.

During the past ten years there have been legislative efforts made to increase safety to the public and soundness in the state's financial institutions. The chart below shows the statutes that have been added or amended over the past five years. The Department has either proposed or worked closely with the industry to craft legislation to create a better regulatory environment:

<u>Legislative Year</u>	<u>Related Activity</u>	<u>Financial Statutes Modified</u>
2007	Credit Unions	6-352, 6-561
2008	Bank Organization & Regulation	6-246
2008	Collection Agencies	32-1025
2008	State Banking Department	6-128, 6-137
2008	Mortgage Bankers, Brokers, & Loan Originators	6-901, 6-903, 6-904, 6-909, 6-911, 6-943, 6-947, 6-981, 6-991.01–6-991.07
2009	Mortgage Bankers, Brokers, & Loan Originators	6-901, 6-903, 6-904, 6-913, 6-949, 6-991, 6-991.08 – 6-991.22
2009	State Banking Department	6-123, 6-123.01, 6-126
2010	Motor Vehicle	44-291
2010	Data Match & Data Exchange	6-1601
2010	Reverse Mortgages	6-1701 - 6-1708
2010	State Banking Department	6-126, 6-140
2010	Credit Unions	6-510
2011	State Banking Department	6-122

2011	Escrow Agents	6-841.01
2011	Mortgage Bankers, Brokers, & Loan Originators	6-912
2011	Motor Vehicle	44-291

The Department's legislative agenda for the 2013 session currently includes five proposals that are technical cleanups. These amendments would serve to provide clarity to licensees, eliminate unnecessary burden, and align with federal law where necessary. These statutory changes will not affect the Department's ability to regulate the financial services industry.

9. The extent to which changes are necessary in the laws of the agency, board, or commission to adequately comply with the factors listed in the sunset law.

Substantial legislative changes are not required for the Department to fulfill its mission of ensuring safety and soundness of state-chartered financial institutions and compliance with statutes applying to entities licensed by the Department.

Exhibit "C" shows the Department's General Fund revenue, appropriation, and actual expenditure history over the past ten years. Since reaching nearly \$4.1 million at the beginning of FY 2008 (reduced to \$3.9M mid-year), DFI's general fund appropriation has been reduced by \$1.2 million. DFI's FY 2013 base appropriation is \$2.9 million - down over 28% from its peak. DFI's 10 year average appropriation is \$3.1 million.

In FY 2011, DFI also began receiving an appropriation from the newly established Financial Services Fund, to fund the costs associated with running a new Loan Originator licensing program. The FY 2013 budget for this fund is \$923K.

Despite the additional FTE authorized for the new loan originator licensing program (Financial Services Fund) the number of licensees per FTE has more than doubled since FY 2009 (see Exhibit B). While the number of licensees (excluding loan originators) has declined since 2003 – due to the prolonged economic downturn and mortgage crisis - the addition of 5,320 licensed Loan Originators caused the number of licensees per FTE to jump to 149, from 64 just three years earlier. That number is projected to grow to 162 per FTE for FY 2013. (Note: When based on 48 actual "funded" FTE, the projected ratio spikes to 196 for FY 2013).

10. The extent to which the termination of the agency, board, or commission would significantly harm the public health, safety or welfare.

Regulation of the financial services industry is critical to the protection of business and the public in transactions that can significantly affect financial welfare. Termination of the Department would cause harm to the public by increasing exposure to deceptive practices by enterprises (most particularly mortgage bankers and brokers, money

transmitters, escrow agents, sales finance companies and collection agencies) and reducing control over financial institutions (banks, credit unions, and trust companies).

Furthermore, the regulated industries would also be harmed as consumers would take their business to other states where the enterprises are licensed and supervised.

The Department remains the only state regulatory authority responsible for financial enterprises currently regulated by the agency and potentially posing economic risks to the public. Though the Department shares the oversight responsibility with federal regulators (Federal Deposit Insurance Corporation, Federal Reserve Bank, National Credit Union Administration, and the Consumer Financial Protection Bureau), it remains the primary regulator and is ultimately responsible for the safety and soundness of Arizona institutions. A failure of any of these institutions would have a widely-dispersed and widely-felt economic impact on the State and could potentially affect credit rating, resulting in added borrowing costs. There are no other nonprofit or private enterprises that administer the same functions as the Department.

There are agencies in every state across the country that performs a comparable function to the Arizona Department of Financial Institutions. Exhibit "D" is a contact list provided by the Conference of State Bank Supervisors (CSBS) for state agencies that have a similar function to AzDFI.

11. The extent to which the level of regulation exercised by the agency, board, or commission compares to other states and is appropriate and whether less or more stringent levels of regulation would be appropriate.

The level of regulation exercised by the Arizona Department of Financial Institutions compares with that of departments in other states. The Department strives for strong supervision and fair application of rules and statutes that are conducive to a progressive business climate. The Department's mission is to ensure the safety of the Arizona consumer and soundness for the Arizona business.

12. The extent to which the agency, board, or commission has used private contractors in the performance of its duties and how more effective use of private contractors could be accomplished.

The Department has employed private contractors as needed over the past decade. The primary reason for this is to assist in the completion of examinations and other statutory requirements. There have been periods of time that the Department has not had resources it has been accustomed to, which prompted a measure of organizational change. One drawback to contract examiners has been finding the appropriate skill set for complex examinations.

Without the ability to hire additional full time employees, the Department has contracted professionals in different capacities as needed. The Department has Interagency Service Agreements (ISAs) with agencies such as the Attorney General's Office and the Department of Real Estate. AzDFI has acted on an ISA with the Department of Real Estate to share a Legislative Liaison, 50/50, since 2010.

For general office supply and equipment, the Department purchases from ADOA's State Procurement Office's statewide contracted vendors. No office products or overhead services are made or performed 'in house' other than building maintenance services provided by ADOA.

The Department has few opportunities for further transferring of expenditures from the public realm to the private sector. A significant amount of our appropriation is allocated to Personnel Services, Employee Related Expense (ERE), Rent, and Risk Management expense. Since ERE, Rent, and Risk Management are all legislatively-derived expense items, the only available 'outsourcing opportunity' is Personnel Services (i.e. employee payroll).

The Department's work output is confidential as a matter of statute and of sound policy. Department work papers and findings are considered confidential according to A.R.S. § 6-129 and cannot be disclosed to parties that are not connected to the Department.

- 13. The extent to which the Agency, board, or commission potentially creates unexpected negative consequences that might require additional review by the Committee of Reference, including increasing the price of goods, affecting the availability of services, limiting the abilities of individuals and businesses to operate efficiently, and increasing the cost of government.**

The Department continues to be paper intensive which causes licensees additional cost and time to complete initial and renewal applications. While the agency continues to streamline all work processes, much greater attention is required which will result in higher costs to state government.

**License Activity Summary
For 09/06/2012**

License Type	09/04/2012 Count	Approved	Closed	Revoked	Suspended	Calc. Count	09/06/2012 Count	Branch Count
Advance Fee Loan Broker	41					41	41	
Bank	18					18	18	64
Collection Agency	705					705	706	23 X
Commercial Mortgage Banker	12					12	12	6
Commercial Mortgage Broker	52					52	52	
Consumer Lender	34					34	34	129
Credit Union	20					20	20	123
Debt Management Company	35					35	36	17 X
Escrow Agent	101					101	101	362
Loan Originators	5,683					5,683	5,697	
Money Transmitter	69					69	69	157
Mortgage Banker	287					287	287	897
Mortgage Broker	366					366	366	266
Motor Vehicle Dealer	613					613	613	134
Pre-Need Funeral Trust	25					25	25	
Premium Finance Company	34					34	34	5
Registered Exempt Person	1					1	1	
Sales Finance Company	451					451	450	546 X
Trust Company	3					3	3	
Trust Division								
Totals for 09/06/2012	8,550	0	0	0	0	8,550	8,565	2,729 X

Department of Financial Institutions: Doing More with Less, Fiscal Years 2003 through 2012

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Licensed Enterprises (ex. Loan Originators)	3,126	3,401	3,759	4,165	4,275	4,161	3,619	3,049	2,818	2,832
Licensed Loan Originators	-	-	-	-	-	-	-	1,975	4,821	5,320
State Chartered Banks	29	31	32	34	31	34	34	24	21	18
State Chartered Credit Unions	30	31	29	27	27	26	26	23	22	20
Total Number Regulated	3,185	3,463	3,820	4,226	4,333	4,221	3,679	5,071	7,682	8,190
Employees (Authorized FTEs):										
General Fund	48.1	48.1	48.1	53.1	55.1	57.1	57.1	47.1	46.1	46.1
Financial Services Fund	-	-	-	-	-	-	-	-	9.0	9.0
Authorized FTE	48.1	48.1	48.1	53.1	55.1	57.1	57.1	47.1	55.1	55.1
Number of Licensees per FTE	66	72	79	80	79	74	64	108	139	149

Note: Data reflect fiscal year-end counts.

Arizona Department of Financial Institutions: General Fund Revenue and Expenditure Performance vs. Budget, Fiscal Years 2003-2012.

Despite the ongoing economic downturn, DFI's revenue less expenditures added \$1.6M to the state's general fund in FY 2012.

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	10 Year Average
Revenue	5,481,942	5,896,000	6,741,754	7,427,882	8,149,262	6,096,763	5,435,509	4,637,690	4,412,390	4,302,145	5,858,134
Appropriation	2,716,100	2,736,000	2,891,700	3,316,000	3,733,900	3,883,300	3,304,900	2,970,300	2,894,800	2,814,300	3,126,130
Expenditures	2,707,150	2,721,500	2,856,834	3,308,741	3,665,280	3,882,742	3,304,393	2,970,197	2,794,887	2,745,082	3,095,681
Net to General Fund (Revenue less Expenditures)	2,774,792	3,174,500	3,884,920	4,119,141	4,483,982	2,214,021	2,131,116	1,667,494	1,617,502	1,557,063	2,762,453

Note: Revenue comes from examinations and licensing fees as well as annual assessments paid by banks and credit unions.

EXHIBIT C

**ARIZONA DEPARTMENT OF FINANCIAL INSTITUTIONS
FY 2009 AND FY 2010 BUDGET REDUCTIONS
IMPACT ON EXAMINER POSITIONS**

License Type	Current Number of Licensees (as of 6/30/12)	Examiner Staff Before FY 2009 Budget Cuts	Examiner Staff Before FY 2009 Budget Cuts	Examiner Staff Before FY 2009 Budget Cuts	Current FY 2013 Examiner Staff	Current FY 2013 Examiner Staff	Current FY 2013 Examiner Staff
Financial Institutions:							
Banks (18) and Trust Cos. (3)	21	4	0	4	10	0	10*
Credit Unions	20	4	0	4			
Financial Enterprises:							
Mortgage Brokers and Bankers	709	5	4	9	2	0	2
Loan Originators	5,320	0	0	0	0	3	3
Escrow Agents	101	4	2	6	2	0	2
Collection Agents	697	1	0	1	1	0	1
Payday Lenders	0	1	0	1	0	0	0
Consumer Lender	34	0	0	0	0	0	0
Sales Finance Cos **	458	0	0	0	0	0	0
MV Dealers **	625	0	0	0	0	0	0
Money Transmitter **	69	0	2	2	0	1	1
All Other	136	0	0	0	0	0	0
Sub-Total	8,190	19	8	27	15	4	19
Consumer Affairs Division		5	0	5	3	0	3
Total Examiner Positions		24	8	32	18	4	22
Reduction in Examiners (%)		N/A	N/A	N/A	25%	50%	31%

* Effective 7/01/11, the Bank & Credit Union Divisions were merged into a single Division, comprised of a pool of 10 Financial Institutions examiners.
 ** License type not statutorily required to be examined by DFI (A.R.S. § 6-122.D).

State Banking Departments

State Banking Departments

State Banking Department	State Bank Supervisor	Address & Phone
Alabama State Banking Department	Mr. John D. Harrison Superintendent of Banks	PO Box 4600 Montgomery, AL 36103-4600 Phone: (334) 242-3452 Fax: (334) 242-3500
Alaska Division of Banking and Securities	Ms. Lorie Hovanec Director	PO Box 110807 Juneau, AK 99811-0807 Phone: (907) 465-2521 Fax: (907) 465-1231
Arizona Department of Financial Institutions	Mr. Lauren Kingry Superintendent	2910 North 44th Street Phoenix, AZ 85018 Phone: (602) 771-2800 Fax: (602) 381-1225
Arkansas State Bank Department	Ms. Candace A. Franks Bank Commissioner	400 Hardin Road, Suite 100 Little Rock, AR 72211 Phone: (501) 324-9019 Fax: (501) 324-9028
California Department of Financial Institutions	Ms. Teveia R. Barnes Commissioner	45 Fremont Street San Francisco, CA 94105-2219 Phone: (415) 263-8500 Fax: (415) 288-8830
Colorado Division of Banking	Mr. Fred Joseph State Bank Commissioner	1560 Broadway, Suite 975 Denver, CO 80202 Phone: (303) 894-7575 Fax: (303) 894-7570
Connecticut Department of Banking	Mr. Howard F. Pitkin Banking Commissioner	260 Constitution Plaza Hartford, CT 06103-1800 Phone: (860) 240-8299 Fax: (860) 240-8178

State Banking Departments

Delaware Office of the State Bank Commissioner	Mr. Robert A. Glen State Bank Commissioner	555 E. Loockerman Street Dover, DE 19901 Phone: (302) 739-4235 Fax: (302) 739-3609
District of Columbia Department of Insurance, Securities and Banking	Mr. William P. White Commissioner	810 First Street NE Washington, DC 20002 Phone: (202) 727-8000 Fax: (202) 535-1194
Florida Office of Financial Regulation	Ms. Linda B. Charity Interim Commissioner	200 East Gaines Street Tallahassee, FL 32399-0370 Phone: (850) 410-9800 Fax: (850) 410-9548
Georgia Department of Banking & Finance	Mr. Robert M. Braswell, CEM Commissioner	2990 Brandywine Road, Suite 200 Atlanta, GA 30341-5565 Phone: (770) 986-1633 Fax: (770) 986-1654
Guam Department of Revenue and Taxation	Mr. Artemio B. Ilagan Banking & Insurance Commissioner	PO Box 23607 GMF, GU 96921 Phone: (671) 635-1817 Fax: (671) 633-2643
Hawaii Division of Financial Institutions	Ms. Iris Ikeda Catalani Commissioner of Financial Institutions	PO Box 2054 Honolulu, HI 96805 Phone: (808) 586-2820 Fax: (808) 586-2818
Idaho Department of Finance	Mr. Gavin M. Gee Director of Finance	PO Box 83720 Boise, ID 83720-0031 Phone: (208) 332-8000 Fax: (208) 332-8097
Illinois Department of Financial & Professional Regulation - Division of Banking	Mr. Manuel Flores Director, Division of Banking	320 West Washington Street Springfield, IL 62786 Phone: (217) 785-2900 Fax: (217) 557-0330

State Banking Departments

Indiana Department of Financial Institutions	Mr. David H. Mills Director	30 South Meridian Street Indianapolis, IN 46204 Phone: (317) 232-3955 Fax: (317) 232-7655
Iowa Division of Banking	Mr. James M. Schipper Superintendent of Banking	200 East Grand Avenue Des Moines, IA 50309-1827 Phone: (515) 281-4014 Fax: (515) 281-4862
Kansas Office of the State Bank Commissioner	Mr. Ed Splichal Commissioner	700 SW Jackson Street, Suite 300 Topeka, KS 66603 Phone: (785) 296-2266 Fax: (785) 296-0168
Kentucky Department of Financial Institutions	Mr. Charles A. Vice Commissioner	1025 Capital Center Drive Frankfort, KY 40601 Phone: (502) 573-3390 Fax: (502) 573-8787
Louisiana Office of Financial Institutions	Mr. John P. Ducrest, CEM Commissioner of Financial Institutions	PO Box 94095 Baton Rouge, LA 70804-9095 Phone: (225) 925-4660 Fax: (225) 925-4548
Maine Bureau of Financial Institutions	Mr. Lloyd P. LaFountain, III Superintendent	36 State House Station Augusta, ME 04333-0036 Phone: (207) 624-8570 Fax: (207) 624-8590
Maryland Office of Financial Regulation	Mr. Mark Kaufman Commissioner	500 North Calvert Street Baltimore, MD 21202 Phone: (410) 230-6100 Fax: (410) 333-0475
Massachusetts Division of Banks	Mr. David J. Cotney Commissioner	1000 Washington Street Boston, MA 02118-6400 Phone: (617) 956-1500

State Banking Departments

Michigan Office of Financial and Insurance Regulation	Mr. Kevin Clinton Commissioner	PO Box 30220 Lansing, MI 48909-0220 Phone: (517) 373-6950 Fax: (517) 335-0908
Minnesota Department of Commerce	Mr. Michael Rothman Commissioner	85 7th Place East, Suite 500 St. Paul, MN 55101-2198 Phone: (651) 296-2135 Fax: (651) 296-8591
Mississippi Department of Banking and Consumer Finance	Mr. Jerry T. Wilson Commissioner	PO Drawer 23729 Jackson, MS 39225-3729 Phone: (601) 359-1031 Fax: (601) 359-3557
Missouri Division of Finance	Mr. Richard J. Weaver, CEM Commissioner	PO Box 716 Jefferson City, MO 65102 Phone: (573) 751-3242 Fax: (573) 751-9192
Montana Division of Banking & Financial Institutions	Ms. Melanie S. Hall Commissioner	PO Box 200546 Helena, MT 59620-0546 Phone: (406) 841-2920 Fax: (406) 841-2930
Nebraska Department of Banking and Finance	Mr. John Munn Director of Banking & Finance	PO Box 95006 Lincoln, NE 68509 Phone: (402) 471-2171 Fax: (402) 471-3062
Nevada Financial Institutions Division	Mr. George E. Burns Commissioner	2785 E. Desert Inn Road Las Vegas, NV 89121 Phone: (702) 486-4120 Fax: (702) 486-4563
New Hampshire State Banking Department	Mr. Ronald A. Wilbur Commissioner	53 Regional Drive Concord, NH 03301 Phone: (603) 271-3561 Fax: (603) 271-1090

State Banking Departments

New Jersey Department of Banking and Insurance	Mr. Ken Kobylowski Acting Commissioner	PO Box 040 Trenton, NJ 08625-0040 Phone: (609) 292-7272 Fax: (609) 777-0107
New Mexico Financial Institutions Division	Ms. Cynthia Richards Director	PO Box 25101 Santa Fe, NM 87504 Phone: (505) 476-4885 Fax: (505) 476-4670
New York State Department of Financial Services	Mr. Benjamin Lawskey Superintendent of Financial Services	One State Street Plaza New York, NY 10004-1511 Phone: (212) 709-3530 Fax: (212) 709-3520
North Carolina Office of Commissioner of Banks	Mr. Ray Grace, CEM Acting Commissioner of Bank	4309 Mail Service Center Raleigh, NC 27699-4309 Phone: (919) 733-3016 Fax: (919) 733-6918
North Dakota Department of Financial Institutions	Mr. Robert J. Entringer, CEM Commissioner	2000 Schafer Street, Suite G Bismarck, ND 58501-1204 Phone: (701) 328-9933 Fax: (701) 328-0290
Northern Mariana Islands Department of Commerce	Mr. Sixto K. Igisomar Deputy Secretary of Commerce, Acting Commissioner	Caller Box 10007 Saipan, MP 96950 Phone: (670) 664-3000 Fax: (670) 664-3067
Ohio Division of Financial Institutions	Mr. Charles J. Dolezal Superintendent of Financial Institutions	77 South High Street Columbus, OH 43215-6120 Phone: (614) 728-8400 Fax: (614) 752-9029
Oklahoma State Banking Department	Mr. Mick Thompson Bank Commissioner	2900 N. Lincoln Blvd Oklahoma City, OK 73105 Phone: (405) 521-2782 Fax: (405) 522-2993

State Banking Departments

Oregon Division of Finance & Corporate Securities	Mr. David C. Tatman Administrator	PO Box 14480 Salem, OR 97309-0405 Phone: (503) 378-4140 Fax: (503) 947-7862
Pennsylvania Department of Banking	Mr. Glenn Moyer Secretary	17 N. Second Street Harrisburg, PA 17101-2290 Phone: (717) 787-2665 Fax: (717) 787-8773
Puerto Rico Office of the Commissioner of Financial Institutions	Mr. Rafael Blanco, Esq. Commissioner	PO Box 11855 San Juan, PR 00910-3855 Phone: (787) 723-3131 Fax: (787) 723-4042
Rhode Island Department of Business Regulation	Mr. Paul McGreevy Director of the Department of Business Regulation	1511 Pontiac Avenue Cranston, RI 02920 Phone: (401) 462-9503 Fax: (401) 462-9532
South Carolina State Board of Financial Institutions	Mr. Louie A. Jacobs Commissioner of Banking	1205 Pendleton St., Ste 305 Columbia, SC 29201 Phone: (803) 734-2001 Fax: (803) 734-2013
South Dakota Division of Banking	Mr. Bret Afdahl Director	217 1/2 W. Missouri Ave. Pierre, SD 57501-4590 Phone: (605) 773-3421 Fax: (866) 326-7504
Tennessee Department of Financial Institutions	Mr. Greg Gonzales Commissioner	414 Union Street Nashville, TN 37219 Phone: (615) 741-2236 Fax: (615) 741-2883
Texas Department of Banking	Mr. Charles G. Cooper Banking Commissioner	2601 North Lamar Blvd. Austin, TX 78705-4294 Phone: (512) 475-1323 Fax: (512) 475-1313

State Banking Departments

Utah Department of Financial Institutions	Mr. G. Edward Leary Commissioner of Financial Institutions	PO Box 146800 Salt Lake City, UT 84114-6800 Phone: (801) 538-8830 Fax: (801) 538-8894
Vermont Department of Financial Regulation	Mr. Steve Kimbell Commissioner	89 Main Street Montpelier, VT 05620-3101 Phone: (802) 828-3307 Fax: (802) 828-1477
Virgin Islands Division of Banking and Insurance	Mr. Gregory R. Francis Lt. Governor, Commissioner, Division of Banking & Insurance	Kongens Gade #5049 St. Thomas, VI 00802 Phone: (340) 774-7166 Fax: (340) 774-9458
Virginia Bureau of Financial Institutions	Mr. Edward J. Face, CEM Commissioner of Financial Institutions	PO Box 640 Richmond, VA 23218-0640 Phone: (804) 371-9657 Fax: (804) 371-9416
Washington Department of Financial Institutions	Mr. Scott Jarvis Director Financial Institutions	PO Box 41200 Olympia, WA 98504-1200 Phone: (360) 902-8704 Fax: (360) 753-6070
West Virginia Division of Financial Institutions	Ms. Sara M. Cline Commissioner of Financial Institutions	900 Pennsylvania Avenue Charleston, WV 25302-3542 Phone: (304) 558-2294 Fax: (304) 558-0442
Wisconsin Department of Financial Institutions	Mr. Peter J. Bildsten Secretary, Department of Financial Institutions	PO Box 8861 Madison, WI 53707-8861 Phone: (608) 264-7800 Fax: (608) 261-4334
Wyoming Division of Banking	Mr. Albert L. Forkner, CEIC Commissioner	Herschler Building, 3rd Fl. East Cheyenne, WY 82002 Phone: (307) 777-7797

NOTICE OF FINAL RULEMAKING
TITLE 20. COMMERCE, FINANCIAL INSTITUTIONS, AND INSURANCE
CHAPTER 4. DEPARTMENT OF FINANCIAL INSTITUTIONS

PREAMBLE

1.

<u>Article, Part or Section Affected (as applicable)</u>	<u>Rulemaking Action</u>
R20-4-102	Amend
Table A	Amend
R20-4-927	New Section
R20-4-928	New Section
R20-4-1813	New Section

2. **Citations to the agency's statutory rulemaking authority to include both the authorizing statute (general) and the implementing statute (specific):**

Authorizing statute: A.R.S. § 6-123(2)

Implementing statute: A.R.S. §§ 6-949, 6-912, and 6-913

3. **The effective date of the rule:**

Sixty days after a certified original and two copies of the rule and preamble are filed in the office of the Secretary of State by the Governor's Regulatory Review Council in accordance with A.R.S. § 41-1032.

4. **Citations to all related notices published in the *Register* as specified in R1-1-409(A) that pertain to the record of the final rulemaking package:**

Notice of Rulemaking Docket Opening: 17 A.A.R. 1361, July 22, 2011

Notice of Proposed Rulemaking: 18 A.A.R. 881 April 13, 2012

5. **The agency's contact person who can answer questions about the rulemaking:**

Name:	Richard Fergus
Address:	2910 N. 44th St., Suite 310
	Phoenix, AZ 85018
Telephone:	(602) 771-2783
Fax:	(602) 381-1225
E-mail:	rfergus@azdfi.gov
Web site:	www.azdfi.gov

6. **An agency's justification and reason why a rule should be made, amended, repealed or renumbered, to include an explanation about the rulemaking:**

The purpose for initiating these rules is to implement legislative changes over the past three years. One of those legislative changes was the passage of HB2318 (mortgage bankers; loan originators; fees), which was signed by Governor Brewer on July 13, 2009. The bill amended A.R.S. § 6-949 to require that the Department establish the application process for converting a mortgage banker license to a mortgage broker license. R20-4-1813 is intended to provide this conversion process.

A second legislative change was the passage of HB2004 (commercial mortgage brokers; license conversion), which was signed by Governor Brewer on April 6, 2011. The bill added A.R.S. § 6-913, requiring that the Department establish a process in rule that allows for mortgage brokers to convert their license to a commercial mortgage broker license. R20-4-927 is intended to provide this conversion process.

A third legislative change occurred with the passage of HB2296 (national banks; mortgage loan originators), which was signed by Governor Brewer on April 19, 2011. The Department is now authorized in A.R.S. § 6-912 to "...charge a fee for processing the original or renewal application for a certificate of exemption and for other costs incurred by the Department." The purpose of R20-4-928 is to implement the fees that the Department will charge in response to this statute, as well as provide the process for applying for and renewing a certificate of exemption. Further, R20-4-102 is being amended to define "exclusive contract" as it is used in A.R.S. §§ 6-912 and 6-991.02. Additionally, R20-4-102 is being amended to add a numbering system that will create ease in identifying definitions established by rule.

Finally, with these legislative changes, as well as the sunset of the deferred presentment company ("payday lender") statutes in 2010, and changes to the loan originator statutes in 2009, it was necessary to amend Table A. Licensing Time-frames to include new license type time frames and delete those which no longer exist.

7. **A reference to any study relevant to the rule that the agency reviewed and either relied on or did not rely on in its evaluation of or justification for the rule, where the public may obtain or review each study, all data underlying each study, and any analysis of each study and other supporting material:**

The Department has not reviewed, and did not rely on, any study as an evaluation or justification for the proposed rules.

8. **A showing of good cause why the rulemaking is necessary to promote a statewide interest if the rulemaking will diminish a previous grant of authority of a political subdivision of this state:**

Not applicable

9. **A summary of the economic, small business, and consumer impact:**

The Department's current projection is that there will be less than 5 entities that apply and qualify for the certificate of exemption to supervise loan originators; therefore it is unlikely that the addition of this registration will result in an increase to state revenues. However, even one applicant for the certificate of exemption, opens up the possibility for at least 200 individuals to obtain their loan originator license. This will have a minimal, yet notable

impact on private employment in Arizona and could potentially raise the revenues generated from loan originator licensing.

The ability for a mortgage broker to be able to convert to a commercial mortgage broker license and only pay the applicable renewal fees for the newly acquired license type will be a substantial savings for the private business, not only financially but also with regard to their time. Rather than having to start as an original applicant for a commercial mortgage broker license and pay the original application and licensing fees, mortgage brokers will be permitted to pay only the renewal fees upon converting the license. This could result in an individual savings for each entity of \$800 for the application fee, the applicable prorated licensing fee, and \$250 for each branch. Further, there will be an additional savings by not having to pay for and attend continuing education courses every year. The overall economic impact of these rules on private and public business is projected to be minimal.

10. A description of any changes between the proposed rulemaking, to include supplemental notices, and the final rulemaking:

Only minor, non-substantive grammatical, formatting, and clarifying changes were made between the proposed that the final rulemaking at the request of GRRC staff.

11. An agency's summary of the public or stakeholder comments made about the rulemaking and the agency response to the comments:

No comments were submitted.

12. All agencies shall list other matters prescribed by statute applicable to the specific agency or to any specific rule or class of rules. Additionally, an agency subject to Council review under A.R.S. §§ 41-1052 and 41-1055 shall respond to the following questions:

a. Whether the rule requires a permit, whether a general permit is used and if not, the reasons why a general permit is not used:

Licensees affected fall within the definition of general permit in A.R.S. § 41-1001 (10).

b. Whether a federal law is applicable to the subject of the rule, whether the rule is more stringent than federal law and if so, citation to the statutory authority to exceed the requirements of federal law:

The rules are promulgated under state law.

c. Whether a person submitted an analysis to the agency that compares the rule's impact of the competitiveness of business in this state to the impact on business in other states:

None

13. A list of any incorporated by reference material as specified in A.R.S. § 41-1028 and its location in the rule:

There is no material incorporated by reference in these rules.

14. Whether the rule was previously made, amended or repealed as an emergency rule. If so, cite the notice published in the Register as specified in R1-1-409(A). Also, the agency shall state where the text was changed between the

emergency and the final rulemaking packages:

Not applicable

15. The full text of the rules follows:

TITLE 20. COMMERCE, FINANCIAL INSTITUTIONS, AND INSURANCE

CHAPTER 4. DEPARTMENT OF FINANCIAL INSTITUTIONS

ARTICLE 1. GENERAL

Section

R20-4-102. Definitions

Table A. Licensing Time-frames

ARTICLE 9. MORTGAGE BROKERS

Section

R20-4-927. Conversion to Commercial Mortgage Broker License

R20-4-928. Certificate of Exemption Application and Renewal

ARTICLE 18. MORTGAGE BANKERS

Section

R20-4-1813. Conversion to Mortgage Broker License

ARTICLE 1. GENERAL

R20-4-102. Definitions

In this Chapter, unless otherwise specified:

1. "Active management" means directing a licensee's activities by a responsible individual, who:
 - a. Is knowledgeable about the licensee's Arizona activities;
 - b. Supervises compliance with:
 - i. The laws enforced by the Department of Financial Institutions as they relate to the licensee, and
 - ii. Other applicable laws and rules; and
 - c. Has sufficient authority to ensure compliance.
2. "Affiliate" has the meaning stated at A.R.S. § 6-901.

3. "Attorney General" means the Attorney General or an assistant Attorney General of the state of Arizona.
4. "Branch office" means any location within or outside Arizona, including a personal residence, but not including a licensee's principal place of business in Arizona, where the licensee holds out to the public that the licensee acts as a licensee.
5. "Business of a savings and loan association or savings bank" means receiving money on deposit subject to payment by check or any other form of order or request or on presentation of a certificate of deposit or other evidence of debt.
6. "Compensation" means, in applying that term's definition in A.R.S. §§ 6-901, 6-941, and 6-971, anything received in advance, after repayment, or at any time during a loan's life. This subsection expressly excludes the following items from those definitions of compensation:
 - a. Charges or fees customarily received after a loan's closing including prepayment penalties, termination fees, reinvestment fees, late fees, default interest, transfer fees, impound account interest and fees, extension fees, and modification fees. However, extension fees and modification fees are compensation if the lender advances additional funds or increases the credit limit on an open-end mortgage as part of the extension or modification;
 - b. Out-of-pocket expenses paid to independent third parties including appraisal fees, credit report fees, legal fees, document preparation fees, title insurance premiums, recording, filing, and statutory fees, collection fees, servicing fees, escrow fees, and trustee's fees;
 - c. Insurance commissions;
 - d. Contingent or additional interest, including interest based on net operating income; or
 - e. Equity participation.
7. "Commercial finance transaction," as that term is used in this Section's definitions of the terms "Engaged in the business of making mortgage loans" and "Engaged in the business of making mortgage loans or mortgage banking loans," means a loan made primarily for other than personal, family, or household purposes.
8. "Control of a licensee," as used in A.R.S. §§ 6-903, 6-944, or 6-978, does not include acquiring additional fractional equity interests in a licensee by any person who already has the power to vote 51% or more of the licensee's outstanding voting equity interests.
9. "Correspondent contract," as that term is used in A.R.S. §§ 6-941, 6-943, 6-971, or 6-973, means an agreement between a lender and a funding source under which the funding source may fund, or is required to fund, loans originated by the lender.
10. "Cushion," as that term is used in R20-4-1811 or R20-4-1908, means funds that a servicer or lender may require a borrower to pay into an escrow or impound account before the borrower's periodic payments are available in the account to cover unanticipated disbursements.
11. "Directly or indirectly makes, negotiates, or offers to make or negotiate" and "Directly or indirectly making, negotiating, or offering to make or negotiate," as those phrases are used in A.R.S. §§ 6-901, 6-941, or 6-971, mean:

- a. Providing consulting or advisory services in connection with a mortgage loan transaction, mortgage banking loan transaction, or commercial mortgage loan transaction;
 - i. To an investor, concerning the location or identity of potential borrowers, regardless of whether the person providing consulting or advisory services directly contacts any potential borrowers; or
 - ii. To a borrower, concerning the location or identity of potential investors or lenders; or
- b. Providing assistance in preparing an application for a mortgage loan transaction, mortgage banking loan transaction, or commercial mortgage banking loan transaction, regardless of whether the person providing assistance directly contacts any potential investor or lender; and
- c. Processing a loan; but
- d. “Directly or indirectly makes, negotiates, or offers to make or negotiate” and “Directly or indirectly making, negotiating, or offering to make or negotiate” do not include:
 - i. Providing clerical, mechanical, or word processing services to prepare papers or documents associated with a mortgage loan transaction, mortgage banking loan transaction, or commercial mortgage banking loan transaction;
 - ii. Purchasing, selling, negotiating to purchase or sell, or offering to purchase or sell a mortgage loan, mortgage banking loan, or commercial mortgage banking loan already funded;
 - iii. Making, negotiating, or offering to make additional advances on an existing open-ended mortgage loan, mortgage banking loan, or commercial mortgage loan including revolving credit lines;
 - iv. Modifying, renewing, or replacing a mortgage loan, a mortgage banking loan, or a commercial mortgage loan already funded, if the parties to and security for the loan are the same as the original loan immediately before the modification, renewal, or replacement, and if no additional funds are advanced and no increase is made in the credit limit on an open-ended loan. Replacing a loan means making a new loan simultaneously with terminating an existing loan.

12. “Electronic record” has the meaning stated at A.R.S. § 44-7002(7).

13. “Employee” means a natural person who has an employment relationship with a licensee that is acknowledged by both the person and the licensee, and:

- a. The person is entitled to payment, or is paid, by the licensee;
- b. The licensee withholds and remits, or is liable for withholding and remitting, payroll deductions for all applicable federal and state payroll taxes;
- c. The licensee has the right to hire and fire the employee and the employee’s assistants;
- d. The licensee directs the methods and procedures for performing the employee’s job;
- e. The licensee supervises the employee’s business conduct and the employee’s compliance with applicable laws and rules; and
- f. The rights and duties under subsections ~~(a)~~ (13) (a) through (e) belong to the licensee regardless of whether another person also shares those rights and duties.

14. “Engaged in the business of making mortgage loans,” as that phrase is used in A.R.S. § 6-902, and “engaged in the business of making mortgage loans or mortgage banking loans,” as that phrase is used in A.R.S. § 6-942, mean the direct or indirect making of a total of more than five mortgage banking loans or mortgage loans, or both in a calendar year. Each loan counts only once as of its closing date. A person is not “engaged in the business of making mortgage loans or mortgage banking loans” if the person makes loans solely in commercial finance transactions in which no more than 35% of the aggregate value of all security taken by the investor on the closing date is a lien, or liens, on real property.
15. “Exclusive contract,” as that term is used in A.R.S. §§ 6-912 and 6-991.02, means a written agreement in which a loan originator agrees to perform services as a loan originator subject to supervision and control by a person holding a certificate of exemption issued under A.R.S. § 6-912 on an exclusive basis. The agreement provides that the loan originator is expressly prohibited from performing loan origination or modification services for any other person during the time the agreement is in effect.
16. “Generally accepted accounting principles” has the meaning used by the Financial Accounting Standards Board or the American Institute of Certified Public Accountants.
17. “Holds out to the public,” as used in this Section’s definition of “branch office,” means advertising or otherwise informing the public that mortgage banking loans, commercial mortgage loans, or mortgage loans are made or negotiated at a location. “Holds out to the public” includes listing a location on business cards, stationery, brochures, rate lists, or other promotional items. “Holds out to the public” does not include a clearly identified home or mobile telephone number on a business card or stationery.
18. “Loan,” as that term is used in A.R.S. §§ 6-126(C)(6) and ~~6-126(C)(8); (8)~~, means all loans negotiated or closed, without regard to the location of the real property collateral or type of loan.
19. “Loan Processing” means obtaining a loan application’s supporting documents for use in underwriting.
20. “Person” means a natural person or any legal or commercial entity including a corporation, business trust, estate, trust, partnership, limited partnership, joint venture, association, limited liability company, limited liability partnership, or limited liability limited partnership.
21. “Property insurance,” as that term is used in A.R.S. §§ 6-909 and 6-947, does not include flood insurance as that term is used in the Flood Disaster Protection Act of 1973, as modified by the National Flood Insurance Reform Act of 1994. 42 U.S.C. 4001, et seq.
22. “Reasonable investigation of the background,” as that term is used in A.R.S. §§ 6-903, 6-943, or 6-976 means a licensee, at a minimum:
- a. Collects and reviews all the documents authorized by the Immigration Reform and Control Act of 1986, 8 U.S.C. 1324a;
 - b. Obtains a completed Employment Eligibility Verification (Form I-9);
 - c. Obtains a completed and signed employment application;
 - d. Obtains a signed statement attesting to all of an applicant’s felony convictions, including detailed information regarding each conviction;

- e. Consults with the applicant's most recent or next most recent employer, if any;
 - f. Inquiries regarding the applicant's qualifications and competence for the position;
 - g. If for a loan officer, loan originator, loan processor, branch manager, supervisor, or similar position, obtains a current credit report from a credit reporting agency; and
 - h. Investigates further if any information received in the above inquiries raises questions as to the applicant's honesty, truthfulness, integrity, or competence. An inquiry is sufficient after two attempts to contact a person, including at least one written inquiry.
- 23. "Record" has the meaning stated at A.R.S. § 44-7002(13).
- 24. "Registered to do business in this state" means:
 - a. If an Arizona corporation, it is incorporated under A.R.S. Title 10, Chapter 2, Article 1;
 - b. If a foreign corporation, it either transfers its domicile under A.R.S. Title 10, Chapter 2, Article 2, or obtains authority to transact business in Arizona under A.R.S. Title 10, Chapter 15, Article 1;
 - c. If a business trust, it obtains authority to transact business in Arizona under A.R.S. Title 10, Chapter 18, Article 4;
 - d. If an estate, it acts through a personal representative duly appointed by this state's Superior Court, under the provisions of A.R.S. Title 14, Chapter 3 or 4;
 - e. If a trust, it delivers to the Superintendent an executed copy of the trust instrument creating the trust together with:
 - All the current amendments, or
 - A true copy of the trust instrument certified accurate and complete by a trustee of the trust before a notary public;
 - f. If a general partnership, limited partnership, limited liability company, limited liability partnership, or limited liability limited partnership, it is organized under A.R.S. Title 29;
 - g. If a foreign general partnership, limited partnership, limited liability company, limited liability partnership, or limited liability limited partnership, it is registered with the Arizona Secretary of State's office under A.R.S. Title 29;
 - h. If a joint venture, association, or any entity not specified in this subsection, it is organized and conducts its business in compliance with Arizona law; or
 - i. The entity is exempt from registration.
- 25. "Registered Exempt Person" means a person who is exempt from licensure pursuant to A.R.S. § 6-912 and A.R.S. Title 6, Chapter 9, Articles 1, 2 and 3 as a federally chartered savings bank that is registered with the nationwide mortgage licensing system and registry and holds a certificate of exemption.
- 26. "Resident of this state" means a natural person domiciled in Arizona.
- 27. "Responsible individual" or "responsible person", as those terms are used in A.R.S. §§ 6-903, 6-943, 6-973, and 6-976, means a resident of this state who:

- a. Lives in Arizona during the entire period of designation as the responsible individual on a license;
- b. Is in active management of a licensee's affairs;
- c. Meets the qualifications listed in A.R.S. §§ 6-903, 6-943, or 6-973; and
- d. Is an officer, director, member, partner, employee, or trustee of a licensed entity.

Table A. Licensing Time-frames

No.	License Type	Legal Authority	Administrative Completeness Review (Days)	Substantive Review (Days)	Overall Time- Frame (Days)
1	Bank	A.R.S. § 6-203, et seq.			
	Initial Application	R20-4-211	45	45	90
2	Bank Trust Dept.	A.R.S. § 6-381			
	Initial Application	A.R.S. § 6-203, A.R.S. § 6-204(C)	45	45	90
3	Savings & Loan	A.R.S. § 6-401, et seq.			
	Initial Application	A.R.S. § 6-408, R20-4-327	75	75	150
4	Credit Union	A.R.S. § 6-501, et seq.			

	Initial Application	A.R.S. § 6-506(A)	60	60	120
5	Trust Company	A.R.S. § 6-851, et seq.			
	Initial Application	A.R.S. § 6-854(A)	75	75	150
6	Consumer Lender	A.R.S. § 6-601, et seq.			
	Initial Application	A.R.S. § 6-603(C)	60	60	120
7	Debt Management	A.R.S. § 6-701, et seq.			
	Initial Application	A.R.S. § 6-704(A), R20-4-602(A), R20-4-620(A)	30	30	60
8	Escrow Agent	A.R.S. § 6-801, et seq.			
	Initial Application	A.R.S. § 6-814	60	60	120
9	Mortgage Broker or <u>Commercial Mortgage Broker</u>	A.R.S. § 6-901, et seq.			

	Initial Application	A.R.S. § 6-903(C) & (D)	60	60	120
10	Mortgage Banker	A.R.S. § 6-941, et seq.			
	Initial Application	A.R.S. § 6-943(D)	60	60	120
11	Commercial Mortgage Banker	A.R.S. § 6-971, et seq.			
	Initial Application	A.R.S. § 6-974(A)	60	60	120
12	Acquisition of Control of Financial Institution	R20-4-1602, R20-4-1702			
	Initial Application	A.R.S. § 6-1104	30	30	60
13	Money Transmitter	A.R.S. § 6-1201, et seq.			
	Initial Application	A.R.S. § 6-1204(A)	60	60	120
14	Advance Fee Loan Broker	A.R.S. § 6-1301, et seq.			
	Initial Application	A.R.S. § 6-1303(A)	30	30	60
15	Premium Finance Co.	A.R.S. § 6-1401, et seq.			
	Initial Application	A.R.S. § 6-1402(C)	60	60	120
16	Collection Agency	A.R.S. § 32-1001, et seq.			
	Initial Application	A.R.S. § 32-1021, R20-4-1502	30	15	45
17	Motor Vehicle Dealer	A.R.S. § 44-281, et seq.			
	Dealer <u>Initial</u> Application	A.R.S. § 44-282(B)	30	15	45
18	Sales Finance Co.	A.R.S. § 44-281, et seq.			
	Sales Finance <u>Initial</u> Application	A.R.S. § 44-282(B)	30	15	45
19	Deferred Presentment Company	A.R.S. § 6-1259			
	Initial Application	A.R.S. § 6-1253	60	60	120

EXHIBIT F

<u>19</u>	<u>Certificate of Exemption</u>	<u>A.R.S. § 6-912</u>			
	<u>Initial Application</u>	<u>A.R.S. § 6-912(B)</u>	<u>45</u>	<u>45</u>	<u>90</u>
<u>20</u>	<u>Loan Originators</u>	<u>A.R.S. § 6-991, et seq.</u>			
	<u>Initial Application</u>	<u>A.R.S. § 6-991.04(A)</u>	<u>60</u>	<u>60</u>	<u>120</u>

ARTICLE 9. MORTGAGE BROKERS

R20-4-927. Conversion to Commercial Mortgage Broker License

- A. Under A.R.S. § 6-913, a mortgage broker licensee shall only be permitted to convert his or her license to a commercial mortgage broker license during the renewal period established by A.R.S. § 6-904.
- B. The licensee seeking conversion shall not be subject to the 12 continuing education units as prescribed by A.R.S. § 6-903(V).
- C. The licensee seeking conversion shall submit:
1. The renewal fees required by A.R.S. § 6-126 for commercial mortgage brokers, and
 2. The information and documents required by A.R.S. § 6-903.

R20-4-928. Certificate of Exemption Application and Renewal

- A. Under A.R.S. § 6-912(C), upon application for a certificate of exemption, an applicant shall pay a nonrefundable fee of \$300.
- B. A person holding a certificate of exemption shall pay a renewal fee of \$150.00 on or before December 31 of each year. Certificates of exemption not renewed by December 31 are automatically suspended, and the certificate holder shall not act as a registered exempt person until the certificate is renewed or a new certificate is issued pursuant to A.R.S. § 6-912. While the certificate is suspended, the licensed loan originators sponsored by the registered exempt person may not transact business as a loan originator. A registered exempt person may renew an automatically suspended certificate by paying the renewal fee plus \$25.00 for each day after December 31 that a renewal fee is not received by the Superintendent and applying for renewal as prescribed by the Superintendent. A certificate of exemption that is not renewed by January 31 expires. A certificate of exemption shall not be granted to the holder of an expired certificate of exemption except as provided in A.R.S. § 6-912 for the issuance of an original certificate of exemption. Each licensed loan originator that is sponsored by a registered exempt person whose certificate has expired shall have his or her license placed on inactive status and shall not transact business in Arizona as a loan originator pursuant to A.R.S. § 6-991.02(M).

C. In addition to the application fee, on issuance of the certificate of exemption, the Superintendent shall collect the first year's renewal fee prorated according to the number of quarters remaining until the date of the next annual renewal, as required by A.R.S. § 6-126(B).

D. The following fees are payable to the Department:

1. To change the name of the federally chartered savings bank on a certificate of exemption: \$250.00.
2. To change the responsible individual for the exempt entity: \$250.00.
3. To issue a duplicate or replace a lost certificate of exemption: \$100.00.
4. To change the address of the federally chartered savings bank on a certificate of exemption: \$50.00.

ARTICLE 18. MORTGAGE BANKERS

R20-4-1813. Conversion to Mortgage Broker License

A. Under A.R.S. § 6-949 to apply for a conversion from a mortgage banker license to a mortgage broker license, the applicant shall submit during the renewal period all applicable renewal documents and renewal fees required by A.R.S. §§ 6-126 and 6-903 for mortgage brokers.

REVISED - 10/17/13


REVISED - 10/17/13

REVISED - 10/17/13

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ARIZONA STATE LEGISLATURE

INTERIM MEETING NOTICE OPEN TO THE PUBLIC

SENATE FINANCE AND HOUSE OF REPRESENTATIVES FINANCIAL INSTITUTIONS
COMMITTEE OF REFERENCE FOR
THE PERFORMANCE AUDIT AND THE SUNSET REVIEW OF: 
ARIZONA DEPARTMENT OF FINANCIAL INSTITUTIONS

Date: Monday, October 21, 2013

Time: 1:30 P.M.

Place: HHR 3

AGENDA

1. Call to Order
2. Presentation by the Auditor General
3. Response by the Arizona Department of Financial Institutions
4. Public Testimony
5. Recommendations by the Committee of Reference
6. Adjourn

Members:

Senator Steve Yarbrough, Co-Chair
Senator Olivia Cajero Bedford
Senator Robert Meza
Senator Michele Reagan
Senator Bob Worsley

Representative Kate Brophy McGee, Co-Chair
Representative Jeff Dial
Representative Rosanna Gabaldon
Representative Lydia Hernandez
Representative David Livingston

10/15/13
10/17/13
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People with disabilities may request reasonable accommodations such as interpreters, alternative formats, or assistance with physical accessibility. If you require accommodations, please contact the Chief Clerk's Office at (602) 926-3032, TDD (602) 926-3241.

ARIZONA STATE LEGISLATURE

SENATE FINANCE AND HOUSE OF REPRESENTATIVES FINANCIAL INSTITUTIONS COMMITTEE OF REFERENCE FOR THE PERFORMANCE AUDIT AND THE SUNSET REVIEW OF: ARIZONA DEPARTMENT OF FINANCIAL INSTITUTIONS

Minutes of the Meeting
Monday, October 21, 2013
1:30 p.m., House Hearing Room 3

Members Present:

Senator Steve Yarbrough, Co-Chair
Senator Michele Reagan

Representative Kate Brophy McGee, Co-Chair
Representative Jeff Dial
Representative Lydia Hernandez
Representative David Livingston

Members Absent:

Senator Olivia Cajero Bedford
Senator Bob Worsley
Senator Robert Meza

Representative Rosanna Gabaldon

Staff:

Virginia Carico, House Research Analyst
Bill Ritz, Senate Research Analyst

Co-Chairman Brophy McGee called the meeting to order at 1:37 p.m. and attendance was noted.

Presentation by the Auditor General

Derek Barber, Performance Auditor, Office of the Auditor General, distributed a handout entitled "Arizona Department of Financial Institutions, Performance Audit and Sunset Review" (Attachment A). Mr. Barber gave a powerpoint presentation and answered questions posed by the Committee.

Response by the Arizona Department of Financial Institutions

Lauren W. Kingry, Superintendent, Department of Financial Institutions, introduced the managers of the department and distributed a handout entitled "Arizona Department of Financial Institutions, Sunset Review Presentation, Committee of Reference" (Attachment B) and gave an overview of the response by the Department of

Financial Institutions to the audit performed by the Auditor General's Office. Mr. Kingry answered questions posed by the Committee.

Recommendations by the Committee of Reference

Senator Yarbrough moved that the Committee of Reference make the recommendation to continue the Arizona Department of Financial Institutions for ten years. The motion CARRIED with a voice vote.

Attached is a list noting the individuals who registered their position on agenda items (Attachment C).

There being no further business, the meeting was adjourned at 2:26 p.m.

Respectfully submitted,



Toy Brown
Committee Secretary

(Audio recordings and attachments are on file in the Secretary of the Senate's Office/Resource Center, Room 115. Audio archives are available at <http://www.azleg.gov>)

Arizona Department of Financial Institutions

Performance Audit and Sunset Review

Issued August 2013



Presenter: Derek Barber
Date: October 21, 2013

Madame Chairman members of the committee.

My name is Derek Barber, and I represent the Auditor General's Office.

Today I am presenting information on our performance audit and sunset review of the Arizona Department of Financial Institutions [\[click\]](#)

(Note: Representative Katie Brophy McGee-House Chair, Senator Steve Yarbrough, Senate Chair),

Department history and responsibilities

Established in 1973, formerly the State Banking Department

- Financial institutions like banks and credit unions

- Financial enterprises like collection agencies and sales finance companies

[click]

The Department was established in 1973 to regulate the State's *financial institutions*

[click]

which include state-chartered banks and credit unions as well as [click]

financial enterprises, which include businesses like collection agencies and sales finance companies. [click]

Audit Scope

- Financial enterprise examination program
 - Complaint-handling function
 - Fees
-

Today I will present key findings and recommendations in three areas, including:
[CLICK]

the Department's Financial Enterprise examination program,
[CLICK]

its complaint handling function,
[CLICK]

and its fees .

Finding 1

Department should enhance its
financial enterprise examination
strategy

The first finding was that the Department should enhance its examination strategy by focusing more of its resources on entities found to be a high risk for non-compliance with state laws. [click]

Financial Enterprise Examination Overview

Best practice program features:

- Uses standardized examination checklists
 - Identifies licensee risk
 - Provides licensees with examination results
-

In addition, the Department's enterprise examination program aligns with National Best Practices for Regulatory Agencies in several ways.

[click] For instance, it uses standardized examination checklists,

The Department identifies licensee risk for further non-compliance with state laws to determine how soon a re-examination should occur,

and it provides licensees with examination results.

However, in reviewing the Department's processes for enterprise examinations, we identified four improvement areas.

Area 1: Backlog of statutorily required examinations

- Statute requires examinations of most financial enterprises
- As of October 2012, backlog of 167 exams out of the 933 that were required
- Risk of further growth
- Department conducted full-scope examinations on low-risk entities

Recommendation

- Develop and implement policies to vary the scope of enterprise examinations based on risk
-

First, the Department could take steps to reduce its backlog of financial enterprises requiring an examination.

[click]

Statute requires that most financial enterprises be examined, usually every 5 years.

[click]

In October 2012, the Department had a backlog. Specifically, 167 of 933 enterprises requiring an exam were past due.

[click]

The backlog was at risk of further growth **because in 2010** state law required that Mortgage Loan Originators be licensed and examined every five years. This change more than doubled the Department's total enterprise licensee population.

And, although statute establishes an examination timeframe, the Department's superintendent has the discretion to establish the scope of examinations. [click]
However, when the Department conducts an on-site examination it almost always does a full scope examination, even when an entity had already been identified as low risk based on previous examination results.

[click]

Therefore, the Department should develop and implement policies and procedures to vary the scope of enterprise examinations, especially for entities already found to be

Financial Enterprise Examination Overview

Exams target laws designed to:

- **Protect consumers from financial harm**
 - **Prevent crime**
 - **Assure sound business operations**
-

In fact, the Department's financial enterprise examinations [\[click\]](#) primarily target licensee compliance laws designed to:

1. Protect consumers from financial harm.
2. Prevent or detect financial crimes.
3. And to help ensure that licensees are operating a sound business.

low risk.

Area 2: E-examinations not always administered as intended

- E-exam created to help reduce backlog
 - Self-assessment of compliance
 - No written policies in place
 - In practice, administered to low-risk licensees
-

The second area focused on the Department's electronic examinations, {Click} which it created to help reduce its backlog and began piloting in February 2011. {Click} This type of exam is a licensee's self-assessment of compliance rather than a direct examination.

[click] The Department had not yet developed written policies for administering the e-exam during our review.

[click] However, in practice the e-exam was to be given to low-risk licensees based on previous examination findings.

[click]

Area 2 (cont.): E-examinations not always administered as intended

Not always administered as intended

- E-exam issued to 6 higher risk licensees
- E-exam issued to 800 licensees without a previous on-site exam

Recommendation

- Develop policies for administering the e-exam, and periodically assess whether it is effective at detecting violations
-

[click]

However, the Department did not always issue the e-exam as intended.

[click]

Specifically, the e-exam was issued to at least 6 enterprises that were not considered low risk, and also to at least 800 enterprises that had not previously received an examination.

[click]

Therefore, the Department should develop and implement policies for administering the e-exam, and periodically assess whether it is effective at detecting violations when compared to a more traditional on site examination.

[click]

Area 3: Outdated risk assessment process

- Department assesses risk level following an examination
- Post-examination risk assessment about 20 years old
- Risk-rating worksheets:
 - Categories not consistent
 - Categories not weighted

Recommendation

- Revise risk-assessment worksheets to ensure common risk factors are considered for all licensees and risk factors weighed appropriately.
-

The third area focused on the Department's process for assigning a risk rating after an examination.

[CLICK] The Department assesses risk of further non-compliance after they conduct an examination, but this process has [CLICK] not been reassessed in about 20 years.

[click]

The Department uses risk-rating worksheets to assess the licensee's risk of noncompliance following an examination. For example, a risk rating of 1 represents the lowest risk and 5 represents the greatest risk of further non-compliance.

[click]

The worksheets could be improved since they did not take all risk factors into consideration across licensees, and the risk factors considered were not generally weighted, since less important factors have the same weight as more important factors. For example, the severity of violations could be easily offset by factors like the licensee's preparation for the examination.

[click]

Therefore, the Department should revise its *post-examination* risk assessment worksheets to ensure that all common risk factors are considered for all licensees, and risk factors are appropriately weighed against each other.

Area 4: Followup on examination findings not always adequate

- Followup not usually conducted
 - Department did not follow up on 15 out of 17 examinations
- Department had no policies for conducting followup
- Followup a good way to minimize consumer risk between examinations

Recommendation

- Develop and implement policies for conducting followup
-

The 4th and final area we focused on was the Department's follow-up process after an enterprise examination.

[click]

The Department does not generally follow-up to ensure corrective actions have been taken following an exam, and does not always conduct followup even when more serious violations are identified.

[click]

Specifically, in a random sample of examinations, we found that the Department did not followup on 15 examinations out of 17 where violations were found.

[click]

The Department lacked a formal policy regarding follow-up, such as when it is appropriate to conduct, and to what extent.

[click]

Follow-up is a good way to minimize the compliance risks posed by financial enterprises between exams, which can be as long as five years.

CLICK

Therefore, the Department should develop and implement policies and procedures for conducting followup.

Finding 2

Department should enhance its
complaint-handling process

Our second finding was that the Department should take several steps to ensure that complaints are appropriately processed. [\[click\]](#)

Complaint demographics

Average of 860 complaints per year

Most complaints against

- collection agencies

- mortgage bankers/brokers

- sales finance companies

Case closure commonly result of no violations identified or insufficient evidence presented

According to the Department's complaints data, it received an average of 860 complaints per year between 2010 and 2012.

CLICK

Most complaints were lodged against collection agencies, mortgage bankers and brokers, and sales finance companies for allegations such as harassment or issues related to loan servicing.

CLICK

In addition, most complaints are closed after the Department has found that no violation of law has occurred, or that there was insufficient evidence to corroborate the allegation.

Our review of the complaint handling function identified three improvement areas.

Area 1: Some complaints were not investigated or were inadequately investigated

- Out of 25 randomly selected cases:
 - 2 cases lacked sufficient investigation
 - 2 cases could not be located
 - 2 additional cases were never investigated
 - Policies lacked investigative guidelines
-

First, some complaints were not investigated at all, and the investigation into some other complaints was insufficient to address the issue(s) named in the complaint.
[click]

Specifically , in assessing a sample of 25 complaint cases, we found 2 cases where the Department's investigation was insufficient, and 2 cases that the Department was unable to locate, so we were unable to evaluate the sufficiency of the investigation.
[CLICK]

In addition, 2 more cases were received by the Department but never entered into the its database, and were therefore never investigated.

CLICK

The Department's policies and procedures for complaint handling did not include investigative guidelines, such as the specific steps to take on each investigation.

Area 2: Department did not consistently track unlicensed entities

- Department places unlicensed entities on its Watch List
 - Department did not place at least 3 out of 12 entities on Watch List
-

Our 2nd complaint-handling area focused on the Department's process for tracking potential unlicensed activity:

[click]

The Department uses a tracking system called a Watch List where Department personnel can track entities they suspect have engaged in unlicensed activity but are unable to locate the entity or support the allegation.

[click]

However, we found that three of 12 complaint investigations we reviewed involving unlicensed activity were not conclusive, but the Department had not entered the entities into the Watchlist per their usual practice.

Area 3: Some complaints took a long time to resolve

- Almost half of all complaints resolved within 60 days
 - About 25% open for more than 6 months
 - 5% open for more than a year
-

The third improvement area we identified was in complaint-handling timeliness.

[click]

Although almost half of all complaints were closed within 60 days,

[click]

25% took more than 6 months to resolve,

[click]

and about 5% took over a year

[click]

Recommendations

Modify policies and procedures to:

- Standardize complaint investigation steps
- Establish criteria for documenting suspected unlicensed activity on the Watch List
- Establish and track time frames for resolving complaints

Therefore, the Department should enhance its complaint-handling policies and procedures to ensure that department staff adequately process all complaints in a consistent and timely manner by including

[click]

standardized complaint investigation steps

[click]

, establishing criteria for including entities on the Watch List [click]

, [click]

and analyzing its data to determine an appropriate time frame for resolving complaints.

[click]

Recommendations

Modify policy to enhance a supervisory review process, including:

- Periodic verification that complaints received are investigated
 - Periodic review of timeliness of ongoing investigations
 - Review of investigation sufficiency
-

In addition, the problems with inadequate and untimely investigations highlight a need for the Department to enhance its complaint-handling oversight.

Therefore, the Department should modify its complaint-handling policies and procedures to enhance its supervisory review process.

This process should include

[click] 1) periodic verification that all complaints received are investigated,
[click] 2) A periodic review of the timeliness of ongoing investigations,
[click] and 3) a review of the sufficiency of investigations upon completion.

Finding 3

Department should establish a
structured approach to set
appropriate fees

Our final finding area addressed the Department's need to establish a structured fee setting approach. [\[click\]](#)

Department collects fees

Department has established more than 108 unique fees

- Licensing fees
 - Examination fees
 - Assessment fees on industry assets
-

The Department charges over 100 unique fees to the regulated institutions and enterprises.

[click]

These fees include licensing and examination fees for financial enterprises, and an annual assessment on bank and credit union assets, among others.

Fee Commission Recommendations

- Arizona State Agency Fee Commission report, December 2012
 - Department's fees should be set to generate enough revenue to meet its expenditure needs
 - In fiscal year 2013, contributed \$1.8 million in fee revenue to General Fund
 - Most fees set before 1994
-

{CLICK}

The Arizona State Agency Fee Commission issued a report in December 2012 of their study of the Department's fees.

{CLICK}

They recommended that the Department's fees should be set to generate enough revenue to meet its expenditure needs. Overall the Department generates enough revenue to cover its expenditure needs, but contributes some of its revenue to the General Fund.

[CLICK]

For example, in FY13, it contributed \$1.8 million of its revenues beyond its appropriation

[CLICK]

Since most of the Department's fees have not been changed since before 1994, our goal was to recommend a best practice framework for setting fees.

Recommendations

Best Practices for Fee Setting:

- Assess efficiency of operations
 - Develop a method to determine direct and indirect costs
 - Analyze costs by licensee category to evaluate fee amounts
-

Therefore, the Department should follow best practices for reviewing and revising its fees. Specifically, it should:

[CLICK]

Begin by assessing the efficiency of its operations to ensure that its costs are as low as possible given present resources and technologies, and without sacrificing service quality.

[CLICK]

It should develop and implement a method to determine both its *direct costs*, such as the costs associated with conducting examinations, and *indirect costs*, such as costs incurred in support of operational functions, like administrative support and facility costs.

[CLICK]

The Department should then analyze its fee structure to determine the appropriate fees to charge, and as appropriate, propose legislative changes to its statutory fees.

[CLICK]

Madame Chairman, members of the committee, this concludes my presentation. I am available to answer questions.

Arizona Department of Financial Institutions

Performance Audit and Sunset Review

(Report No. 13-05)

Issued August 2013



Presenter: Derek Barber
Date: October 21, 2013

Madame Chairman, members of the committee, this concludes my presentation. I am available to answer questions.

Arizona Department of
Financial Institutions
Performance Audit and Sunset Review
Issued August 2013



Presenter: Derek Barber
Date: October 21, 2013

Department history and
responsibilities

Established in 1973, formerly the State Banking
Department

- Financial institutions like banks and credit unions

- Financial enterprises like collection agencies and sales
finance companies

Audit Scope

- Financial enterprise examination program
- Complaint-handling function
- Fees

D. H. Chaud

Finding 1

Department should enhance its financial enterprise examination strategy

Financial Enterprise Examination Overview

Exams target laws designed to:

- Protect consumers from financial harm
- Prevent crime
- Assure sound business operations

Financial Enterprise Examination Overview

Best practice program features:

- Uses standardized examination checklists
- Identifies licensee risk
- Provides licensees with examination results

Area 1: Backlog of statutorily required examinations

- Statute requires examinations of most financial enterprises
- As of October 2012, backlog of 167 exams out of the 933 that were required
- Risk of further growth
- Department conducted full-scope examinations on low-risk entities

Recommendation

- Develop and implement policies to vary the scope of enterprise examinations based on risk

Area 2: E-examinations not always administered as intended

- E-exam created to help reduce backlog
- Self-assessment of compliance
- No written policies in place
- In practice, administered to low-risk licensees

Area 2 (cont.): E-examinations not always administered as intended

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Recommendation

- Develop policies for administering the e-exam, and periodically assess whether it is effective at detecting violations

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- Risk-rating worksheets:
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Recommendation

- Revise risk-assessment worksheets to ensure common risk factors are considered for all licensees and risk factors weighed appropriately.

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- Followup a good way to minimize consumer risk between examinations

Recommendation

- Develop and implement policies for conducting followup

Finding 2

Department should enhance its complaint-handling process

Complaint demographics

Average of 860 complaints per year

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Finding 3

Department should establish a structured approach to set appropriate fees

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Fee Commission Recommendations

- Arizona State Agency Fee Commission report, December 2012
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Area 3: Some complaints took a long time to resolve

- Almost half of all complaints resolved within 60 days
- About 25% open for more than 6 months
- 5% open for more than a year

Recommendations

Modify policies and procedures to:

- Standardize complaint investigation steps
- Establish criteria for documenting suspected unlicensed activity on the Watch List
- Establish and track time frames for resolving complaints

Recommendations

Modify policy to enhance a supervisory review process, including:

- Periodic verification that complaints received are investigated
- Periodic review of timeliness of ongoing investigations
- Review of investigation sufficiency

Recommendations

Best Practices for Fee Setting:

- Assess efficiency of operations
- Develop a method to determine direct and indirect costs
- Analyze costs by licensee category to evaluate fee amounts

Arizona Department of
Financial Institutions
Performance Audit and Sunset Review
(Report No. 13-05)
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Findings and Recommendations from the OAG

Arizona Department of Financial Institutions

History

Laws 1973, Chapter 32, established the Arizona Department of Financial Institutions (DFI), formally known as the State Banking Department, to execute all state laws relating to financial institutions and enterprises. DFI supervises and regulates 19 types of financial institutions or enterprises including state-chartered banks, state-chartered credit unions, collection agencies, loan originators, mortgage brokers and sales finance companies. Additionally, DFI investigates complaints filed by consumers against these entities and directs appropriate remedial action if the violations are substantiated.

Arizona Revised Statutes (A.R.S.) § 6-111 stipulates that the chief officer of DFI is the Superintendent who is appointed by the Governor and confirmed by the Senate. The Superintendent is statutorily authorized to supervise and examine state-chartered financial institutions and enterprises and ensure they are operating efficiently, safely and in compliance with applicable state and federal law (A.R.S. § 6-123). Currently, DFI serves approximately 8,000 entities licensed to conduct business in this state (www.azdfi.gov). In FY 2013-14, the baseline operating budget for DFI is approximately \$3.827 million with 58.1 FTE positions.

A.R.S. § 41-3014.10 provides that DFI terminates on July 1, 2014.

Finding 1

- **DFI should enhance its financial enterprise examination strategy:**

DFI should revise its financial enterprise examination strategy to place greater emphasis on high-risk financial enterprises and take steps to improve its risk assessment processes. DFI conducts examinations to ensure that financial enterprises comply with laws designed to protect consumers, prevent financial crimes, and ensure sound business operations. However, as of April 2013, DFI was experiencing a growing backlog of past-due examinations due in part to an increasing number of licensees. Therefore, DFI should adopt a more flexible examination strategy that would enable it to spend less time on compliant financial enterprises and more time with noncompliant or high-risk financial enterprises. Additionally, DFI should improve its risk assessment processes to help ensure it effectively determines an entity's risk for noncompliance and need for examination. Finally, DFI should revise its follow-up process to better ensure serious violations are corrected following an examination.

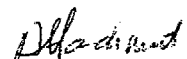
Recommendations:

1.1 DFI should develop and implement written policies and procedures for varying the scope of its examinations based on the financial enterprise's assessed risk. These policies and procedures should identify the types of limited examinations that DFI staff could perform and the risk ratings that would qualify for the limited examinations.

(Administrative)

1.2 To improve the e-exam program, DFI should:

- a. Develop and implement written policies and procedures on when it is appropriate to use e-exams;



- b. Periodically assess whether, when appropriately applied, the e-exam is still effective in detecting violations when compared to the on-site examination; and,
- c. Once formal policies and procedures are established, consider extending the e-exam to other license types to assist in reducing its backlog.

(Administrative)

1.3 DFI should better prioritize the scheduling of financial enterprise examinations to ensure that low-risk licensees are not examined sooner than is needed, while high-risk licenses receive more timely re-examination.

(Administrative)

1.4 DFI should revise its post-examination risk-rating worksheets to ensure risk can be compared across license types. In revising its risk-rating worksheets, DFI should ensure that:

- a. Common risk factors, such as management and controls, are included in all worksheets;
- b. All risk-rating worksheets consider the seriousness of the potential violations; and
- c. Risk factors are appropriately weighed.

(Administrative)

1.5 DFI should enhance its processes for identifying risks prior to an examination, and in doing so, should consider:

- a. Expanding the use of existing financial reports that already submitted by most of its licensees to assess the size and financial performance of licensees compared to their peers; and
- b. Identifying financial products that pose the most financial harm to Arizona consumers.

(Administrative)

1.6 DFI should develop and implement written policies and procedures for conducting follow-ups, including verification of corrective action or re-examination may be necessary. DFI's procedures should identify what types of violations should be followed up on, what level of verification is required, and the time frame for when it should verify that licensees have corrected violations.

(Administrative)

Finding 2

- **DFI should enhance its complaint-handling process:**

DFI should take several steps to ensure that complaints are appropriately processed in a timely manner. DFI is authorized to investigate complaints to determine whether statutory violations have occurred, and it received an average of approximately 860 complaints per year between calendar years 2010-2012. However, DFI's complaint handling process has several weaknesses, including inadequate and untimely complaint investigations, which could affect its ability to protect Arizona consumers and help ensure the soundness of its licensees' business operations. To ensure that complaints are effectively processed, DFI should enhance and/or develop and implement policies and procedures regarding its complaint-handling process, including establishing complaint investigation procedures and complaint-processing time frames. In addition, DFI should enhance its supervisory review process for its complaint-handling

function. Finally, DFI should establish procedures for ensuring the completeness and accuracy of investigative information in its case management system.

Recommendations:

2.1 DFI should enhance its complaint-handling policies and procedures to ensure that staff consistently and adequately process all complaints in a timely manner. Specifically, DFI should:

- a. Standardize complaint investigation steps and include these steps in its policies and procedures;
- b. Establish criteria for documenting suspected unlicensed activity on the Watch List;
- c. Establish and track time frames for resolving complaints, which should include the entire complaint-handling process of opening, investigating, and resolving the complaint, and specific time frames for completing the various steps of its complaint-handling procedures; and
- d. Analyze its complaint-handling data to assist in determining appropriate timeliness goals for resolving complaints, and use the data to identify the specific time frames for completing various steps of its complaint-handling process.

(Administrative)

2.2 DFI should improve its oversight of its complaint-handling function by enhancing its supervisory review process to evaluate the adequacy and timely handling of complaint investigations in a way that is feasible given its available resources, and should document the results of these supervisory reviews in its complaint case files. Specifically, DFI should develop and implement written policies and procedures that require the following:

- a. Verification that all complaints received that are within its jurisdiction are entered into the case management system for investigation;
- b. Periodic review of complain investigations to ensure that these investigations are progressing in a timely manner, documenting these reviews and any associated decisions, and for any cases that have been open for a long time, guidelines on whether they should be further investigated or closed; and
- c. Review of investigation sufficiency to ensure that DFI's investigative policies and procedures are being followed, including reviewing the steps taken to investigate a complaint and ensuring that identified entities are placed on the Watch List.

(Administrative)

2.3 DFI should develop and implement performance measures to ensure that investigators adhere to DFI's investigative time frames, once these time frames have been established.

(Administrative)

2.4 To help ensure the completeness and accuracy of complaint information in its case management system, DFI should:

- a. Update its complaint-handling policies and procedures to include specific definitions for each of its case status designations, including those related to the final outcome of a complaint investigation; and
- b. Develop and implement policies and procedures that require a risk-based review of data entry based on its available resources, including a review of the accuracy of case status designations recorded in the case management system.

(Administrative)

Finding 3

- **DFI should establish a structured approach to set appropriate fees:**

DFI should develop or adopt a structured approach to evaluate the various fees it collects and better align these fees with its costs for providing the associated services. DFI collects over 100 fees, many of which were established before 1988. The Arizona State Agency Fee Commission reviewed DFI's fee structure and recommended DFI's fees be set to match its costs. To implement this recommendation, DFI should take steps to evaluate its current costs and propose legislative or rule changes that would better align its fees with DFI's funding needs, if appropriate.

Recommendations:

3.1 To ensure its fees more fully reflect its costs, DFI should develop a structured approach to evaluate current fees and propose legislative or rule changes that would more closely align its fees with DFI's funding needs. In developing this approach, DFI should do the following:

- a. Assess the efficiency of its operations to ensure costs are as low as possible while considering service quality, and document the results of its assessment. As DFI assesses the efficiency of its operations, it should continue seeking to minimize costs where possible.
- b. Develop and implement a method for estimating DFI's costs, including both direct and indirect costs, and create policies and procedures for using this method.
- c. Establish an allocation methodology for assigning direct payroll costs to licensee category within its currently established accounting system.
- d. After the method is developed and costs are appropriately tracked, DFI should use the costs to analyze its fee structure and determine the appropriate fees to charge.
- e. Include in its policies and procedures a time frame by which it will reevaluate its fees to ensure its fees continue to align with its costs.

(Administrative)

3.2 When warranted and based on its cost and fee assessment, DFI should propose legislative changes to its statutorily established fee amounts or make appropriate rule changes to revise its fees.

(Legislative)

3.3 DFI should consider the effect that the proposed fee changes may have on the affected financial institutions and enterprises and obtain their input when reviewing the fees.

(Administrative)

Arizona Department of Financial Institutions

**Sunset Review Presentation
Committee of Reference
October 21, 2013**



**Janice K. Brewer
Governor**

**Lauren W. Kingry
Superintendent**

Agency Mission

TO LICENSE, EXAMINE, AND SUPERVISE

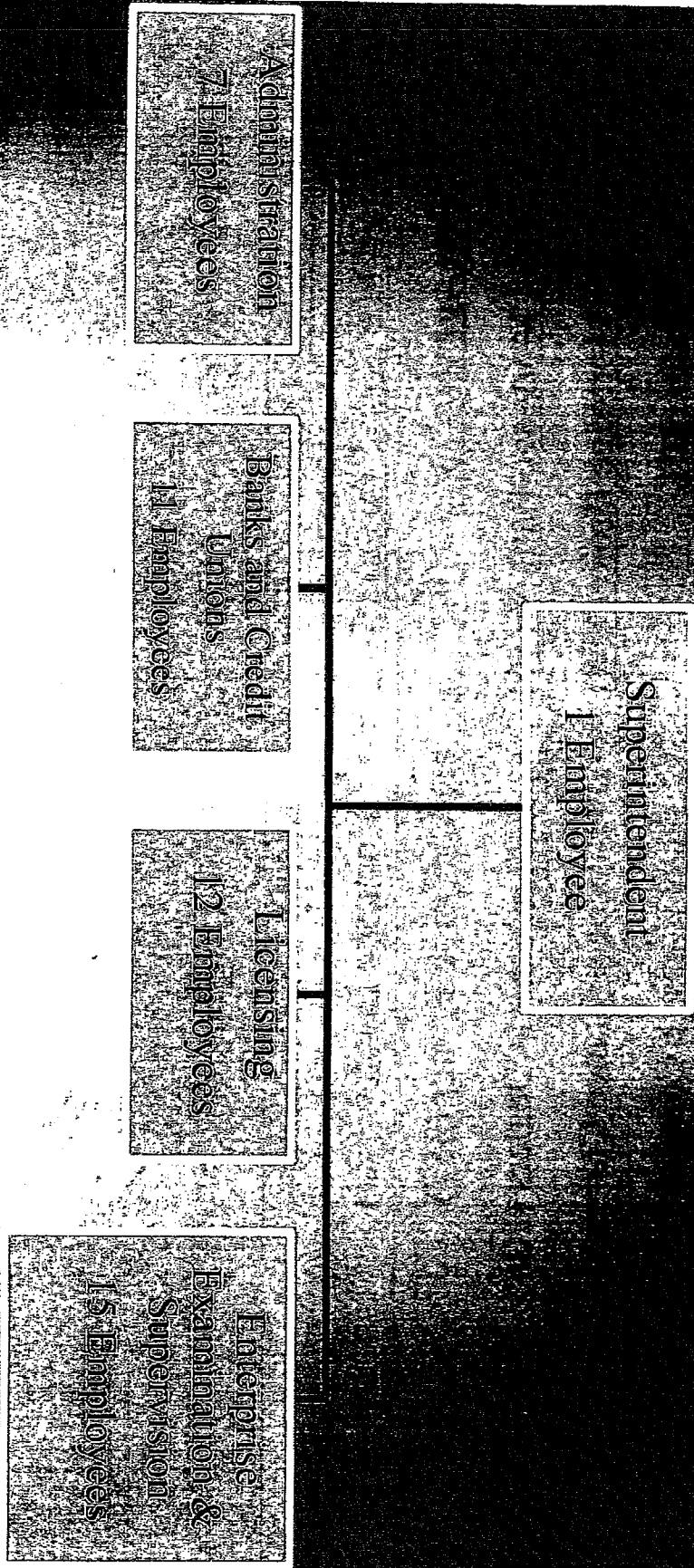
FINANCIAL INSTITUTIONS,

IN COMPLIANCE WITH STATE LAW,

TO ENSURE SAFETY FOR THE ARIZONA CONSUMER
AND

SOUNDNESS FOR THE ARIZONA BUSINESS

Agency Staff Overview



19 Industry License Types

DEPOSITORIES

- Bank (14)
- Credit Union (20)
- Trust Company (3)

NON-DEPOSITORIES

- Advanced Fee Loan Broker (16)
- Collection Agency (734)
- Commercial Mortgage Banker (16)
- Commercial Mortgage Broker (58)
- Consumer Lender (40)
- Debt Management Company (39)

- Escrow Agent (113)
- Pre-Need Funeral Trust (25)
- Loan Originator (7,557)
- Money Transmitter (79)

- Mortgage Banker (325)
- Mortgage Broker (357)
- Motor Vehicle Dealers (704)
- Premium Finance Company (33)
- Sales Finance Company (513)

***Total License Count: 10,670**

Stakeholder Associations

Banks & Credit Unions:

- AZ Bankers Association
- Mountain West Credit Union Association
- Mortgage

AZ Commercial Mortgage

Lenders Association

National Association of

Mortgage Brokers

AZ Association of Mortgage

Professionals

AZ Mortgage Lenders

Association

Financial Enterprises:

- AZ Automobile Dealers Association
- AZ Independent Automobile Dealers Association
- AZ Collectors Association
- Land Title Association of AZ
- AZ Title Loan Association
- AZ Community Financial Services Association
- AZ Escrow Association
- Central AZ Escrow Association

Ariz. Dept. of Financial Institutions Then & Now

	2003	2013	
Banks	30	141	
Credit Unions	31	20	
Trust Companies	4	3	
Depository	65	37	
Non-Depository	3,172	10,641	
All Licensee Branches	3,521	3,310	
Consumer Complaints	1,878	690	
Civil Money Penalties	\$617,000	\$2,244,210	
DEL Staff	52	47	

Sunset Audit Summary

Recommendations

- 3 Enterprise Examination Process
- 2 Consumer Complaint Process
- 3 Administrative Process

IDEI Tomorrow

- RECOVERING ARIZONA ECONOMY
- 500 TO 2,000 NEW LICENSES PER YEAR
- 3 TO 5 NEW LICENSE TYPES
- ELECTRONIC AUTOMATION OF AGENCY
- PRESSURE TO ALIGN WITH FEDERAL AGENCIES